No. 14594

United States Court of Appeals

for the Ninth Circuit

JACK SMITH and ROSE MAE SMITH,
Appellants,

vs.

HARRY C. WESTOVER, former Collector of Internal Revenue and ROBERT A. RIDDELL, Director of Internal Revenue,
Appellees.

Transcript of Record

Appeal from the United States District Court for the Southern District of California, Central Division

FILED
MAR 10 1955
PAUL P. O'BRIEN,
CLERK

Phillips & Van Orden Co., 870 Brannan Street, San Francisco, California—1-26-55

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In the District Court of the United States, Southern District of California, Central Division

No. 15161-Y.

JACK SMITH and ROSE MAE SMITH,
Plaintiffs,

vs.

HARRY C. WESTOVER, former Collector of Internal Revenue, and ROBERT A. RIDDELL, Director of Internal Revenue,
Defendants.

COMPLAINT FOR REFUND OF FEDERAL INCOME TAXES AND INTEREST

Come Now the plaintiffs by their attorneys, Latham & Watkins, and for cause of action against the defendants allege as follows:

I.

Plaintiffs are, and at all times material to this action have been, husband and wife and residents of Los Angeles County, California.

II.

Defendant Harry C. Westover was, from on or about July 1, 1943 to on or about October 31, 1949, Collector of Internal Revenue for the Sixth District of California. Defendant Robert A. Riddell was Acting Collector from on or about October 1, 1949 to on or about April 30, 1950, Collector from on or about May 1, 1950 to on [2] or about Novem-

ber 26, 1952, and, since said last date, Director of Internal Revenue, all for said Sixth District of California.

III.

This action is filed pursuant to the provisions of Title 28, United States Code, Section 1340, for the recovery of income taxes and interest thereon erroneously and illegally collected from plaintiffs by defendants for the calendar years 1943 to 1948, inclusive, together with interest thereon from the dates of payment.

IV.

On or about October 1, 1943, plaintiffs became members of a partnership doing business under the name of Boston Shoe Company. The interest of plaintiff Jack Smith in the profits and losses of said partnership was 40%, and the interest of plaintiff Rose Mae Smith in the profits and losses of said partnership was 30%. The remaining partners were Jack Smith, as Trustee of the Barbara Ann Smith Trust, and Rose Mae Smith, as Trustee of the Howard Samuel Smith Trust, each having a 15% interest in the profits and losses of said partnership. Said partnership kept its books and computed its income on the calendar year basis.

V.

Said partnership was dissolved as of the close of business on December 31, 1944 and, as of January 1, 1945, a second partnership was formed by and between the plaintiffs, the Trusts as aforesaid, and one Herman Weishaupt. The interest of plain-

tiff Jack Smith in the profits and losses of said second partnership was 36%, and the interest of plaintiff Rose Mae Smith in the profits and losses of said second partnership was 27%. The interests of the remaining partners in said profits and losses were 13½% each for Jack Smith, as Trustee of the Barbara Ann Smith Trust, and Rose Mae Smith, as Trustee of the Howard Samuel Smith Trust, and 10% for Herman Weishaupt. Said second partnership kept its books and computed its income on the calendar year basis. [3]

VI.

Said second partnership was dissolved as of the close of business on June 30, 1948 by the withdrawal of said Herman Weishaupt, and, as of July 1, 1948, a third partnership was formed with partners and interests the same as set forth in Paragraph IV herein. Said third partnership continues in existence at the present time, and keeps its books and computes its income on the basis of the fiscal year ending January 31 of each year.

VII.

In each partnership, provision was and is made for salary allowances of $25,000.00 per year to plaintiff Jack Smith and $2,400.00 per year to plaintiff Rose Mae Smith. In the second partnership, provision was also made for a salary allowance of $6,000.00 per year to Herman Weishaupt. Said salary allowances were and are deducted as expenses in arriving at distributable partnership income.

VIII.

In each of his separate Federal income tax returns for the calendar years 1943 to 1946, inclusive, plaintiff Jack Smith reported as income half of his said salary allowance, half of his wife's said salary allowance, and his distributable share of partnership net income computed as above set forth.

IX.

In each of her separate Federal income tax returns for the calendar years 1943 to 1946, inclusive, plaintiff Rose Mae Smith reported as income half of her said salary allowance, half of her husband's said salary allowance, and her distributable share of partnership net income computed as above set forth.

X.

In each of their respective Federal income tax returns for the calendar years 1943 to 1946, inclusive, the said Trusts reported their respective distributable shares of partnership net [4] income computed as above set forth.

XI.

Upon examination of said income tax returns at various times, the Commissioner of Internal Revenue refused to recognize the Trusts as partners and determined that the partnership income so reported by the two trusts should be taxed half to plaintiff Jack Smith and half to plaintiff Rose Mae Smith, and deficiencies in Federal income tax were

assessed against plaintiffs in accordance with such determination.

XII.

Deficiencies of tax and interest assessed were paid by plaintiffs to defendant Harry C. Westover for the calendar years and in the amounts as follows:

Calendar Year	By Plaintiff Jack Smith	By Plaintiff Rose Mae Smith
1943	$ 7,803.23	$ 1,463.27
1944	13,664.16	11,961.54
1945	13,355.14	12,748.92
1946	23,907.98	22,565.80

XIII.

In his separate Federal income tax return for the calendar year 1947, plaintiff Jack Smith reported as income not only half of his said salary allowance, half of his wife's said salary allowance, and his distributable share of partnership net income computed as above set forth, but also half the distributable partnership income of the two trusts.

XIV.

In her separate Federal income tax return for the calendar year 1947, plaintiff Rose Mae Smith reported as income not only half of her said salary allowance, half of her husband's said salary allowance, and her distributable share of partnership income computed as above set forth, but also half the distributable partnership [5] income of the two trusts.

XV.

In their joint Federal income tax return for the calendar year 1948, plaintiffs reported as income not only their said salary allowances and their distributable shares of partnership net income computed as above set forth, but also the distributable partnership income of the two trusts.

XVI.

Plaintiffs' Federal income tax returns for the calendar years 1947 and 1948 were filed with, and the taxes shown thereon to be due were paid to, defendant Harry C. Westover. A deficiency of tax and interest in the amount of $2,955.17, for the calendar year 1948, was paid by plaintiffs to defendant Robert A. Riddell.

XVII.

By reason of the foregoing, plaintiffs have overpaid their Federal income taxes and interest thereon for the calendar years 1943 to 1948, inclusive, in the following total amounts:

By plaintiff Jack Smith.....	$ 56,965.08
By plaintiff Rose Mae Smith...	54,256.32
By plaintiffs jointly	8,557.73
	$119,779.13

All of said amounts were paid to defendant Harry C. Westover except the amount of $2,955.17 for the calendar year 1948 which was paid to defendant Robert A. Riddell.

XVIII.

Plaintiffs duly filed their respective claims for refund on Treasury Department Forms 843 for the calendar years 1943 and 1944 on or about July 19, 1949; for the calendar years 1945 and 1946 on or about May 2, 1950; for the calendar year 1947 on or about March 15, 1951; and for the calendar year 1948 on or about March 15, 1952. In each claim, the reason given in support thereof was that the trusts should be recognized as partners and their [6] shares of the partnership income should be taxed to said trusts rather than to plaintiffs.

XIX.

The Commissioner of Internal Revenue, by registered mail, formally rejected said claims for the calendar years 1943, 1944 and 1945 on or about February 13, 1951 and formally rejected said claims for the calendar year 1946 on or about March 13, 1951. Said claims for the calendar years 1947 and 1948 have not yet been formally acted upon, but more than six months have elapsed since the filing thereof.

Wherefore, plaintiffs pray for judgment against the defendants as follows:

(1) In favor of plaintiff Jack Smith against defendant Harry C. Westover in the amount of $56,-965.08, together with interest thereon as provided by law.

(2) In favor of plaintiff Rose Mae Smith against defendant Harry C. Westover in the amount of

$54,256.32, together with interest as provided by law.

(3) In favor of plaintiffs jointly against defendant Harry C. Westover in the amount of $5,602.56, together with interest as provided by law.

(4) In favor of plaintiffs jointly against defendant Robert A. Riddell in the amount of $2,955.17, together with interest as provided by law.

(5) For costs of suit, and such other relief as the Court may deem proper.

LATHAM & WATKINS,
/s/ By HENRY C. DIEHL,
Attorneys for Plaintiffs [7]

Duly Verified. [8]

[Endorsed]: Filed February 11, 1953.

[Title of District Court and Cause.]

ANSWER

Come now the defendants, by their attorney, Walter S. Binns, United States Attorney for the Southern District of California, and by way of answer to the complaint say:

I.

The allegations contained in paragraph I of the complaint are admitted.

II.

The allegations contained in paragraph II of the complaint are admitted.

III.

The allegations contained in paragraph III of the complaint are admitted, except that it is denied that the taxes and interest collected from the plaintiffs were erroneously or illegally collected. [9]

IV.

The defendants are without information or knowledge sufficient to affirm or deny the allegations contained in paragraph IV of the complaint and they are accordingly denied.

V.

The defendants are without information or knowledge sufficient to affirm or deny the allegations contained in paragraph V of the complaint and they are accordingly denied.

VI.

The defendants are without information or knowledge sufficient to affirm or deny the allegations contained in paragraph VI of the complaint and they are accordingly denied.

VII.

The defendants are without information or knowledge sufficient to affirm or deny the allegations contained in paragraph VII of the complaint and they are accordingly denied.

VIII.

The defendants are at this time without informa-

tion or knowledge sufficient to affirm or deny the allegations contained in paragraph VIII of the complaint and they are accordingly denied.

IX.

The defendants are at this time without information or knowledge sufficient to affirm or deny the allegations contained in paragraph IX of the complaint and they are accordingly denied.

X.

The allegations contained in paragraph X of the complaint are denied.

XI.

The allegations contained in paragraph XI of the complaint are admitted. [10]

XII.

The defendants are at this time without information or knowledge sufficient to affirm or deny the allegations contained in paragraph XII of the complaint and they are accordingly denied.

XIII.

The defendants are at this time without information or knowledge sufficient to affirm or deny the allegations contained in paragraph XIII of the complaint and they are accordingly denied.

XIV.

The defendants are at this time without information or knowledge sufficient to affirm or deny the

allegations contained in paragraph XIV of the complaint and they are accordingly denied.

XV.

The defendants are at this time without information or knowledge sufficient to affirm or deny the allegations contained in paragraph XV of the complaint and they are accordingly denied.

XVI.

The allegations contained in paragraph XVI of the complaint are denied, except that it is admitted that the federal income tax returns of the plaintiffs for the calendar year 1947 were filed with defendant Harry C. Westover.

XVII.

The allegations contained in paragraph XVII of the complaint are denied.

XVIII.

The allegations contained in paragraph XVIII of the complaint are denied, except that it is admitted that the plaintiffs filed claims for refund on Treasury Forms 843 for the calendar year 1943 on July 19, 1949, for the calendar year 1946 on May 2, 1950, and for the calendar year 1947 on March 15, 1951, but each and every allegation contained in said claims for refund filed by the plaintiffs on the above mentioned dates is respectively denied. [11]

XIX.

The allegations contained in paragraph XIX of the complaint are denied, except that it is admitted that on or about February 13, 1951, the Commissioner of Internal Revenue, by registered mail, formerly rejected the claims for refund filed by the plaintiffs for the calendar years 1943, 1944, 1945 and 1946.

Wherefore, the defendants demand judgment that the complaint of the plaintiffs be dismissed and that the defendants be entitled to their lawful costs and disbursements herein.

LAUGHLIN E. WATERS,
United States Attorney
E. H. MITCHELL and
EDWARD R. McHALE,
Assistant U. S. Attorneys,
EUGENE HARPOLE,
Special Attorney, Bureau of
Internal Revenue
/s/ E. H. MITCHELL,
Attorneys for the Defendants [12]

Affidavit of Service by Mail attached. [13]

[Endorsed]: Filed August 19, 1953.

[Title of District Court and Cause.]

MEMORANDUM DECISION

The above-entitled cause heretofore tried, argued and submitted, is now decided as follows:

Judgment will be for the defendants that the plaintiffs take nothing by the Complaint. Costs to the defendants. Findings of Fact and Judgment to be prepared by counsel for the defendants according to Local Rule 7.

Comment

The plaintiffs, Jack Smith and Rose Mae Smith, husband and wife, seek to recover income taxes paid for the years 1943 to 1946, and interest. The claim arises out of a family partnership in the wholesale shoe business known as The Boston Shoe Company, successfully established by the plaintiff Jack Smith before his marriage to the plaintiff Rose Mae Smith. After marriage the spouses considered that the business was community property to which the husband's [14] earning capacity had contributed. On December 31, 1942, the husband bought the wife's interest for the sum of $102,933.89, the purchase price being represented by four promissory notes in different amounts, with different due dates, one year apart, given by him to his wife on the same date.

On September 29, 1943, two trusts were created for the benefit of the children of Jack and Rose Mae Smith, one designated as the "Howard Samuel Smith Trust", in favor of the son then aged eleven;

the other named the "Barbara Ann Smith Trust", in favor of the daughter then aged three. The daughter is still under age. The son is now twenty-two, and, after securing a degree in chemistry at Stanford University, entered Harvard University as a post-graduate student, and now has been accepted at the Harvard Law School. These seemingly minor facts are, in cases of this character, of great importance, because, despite the fact that the son may, during his vacations, have worked in the shoe business, he is not preparing for the business, and it is not likely that a man with such educational background would engage in such business with his father after completing his education.

But back to the Trusts. In creating them, there was assigned by the father to the "Howard Samuel Smith Trust" three United States certificates of indebtedness totaling the principal sum of $30,000.00. To the "Barbara Ann Smith Trust" there was assigned one of the $30,000.00 notes executed by Smith to his wife.

The Trusts are irrevocable. They are subject to the absolute power of the parents as trustees, the beneficiaries having only "the right to enforce" performance. The distribution of the income is controlled by the trustees. [15] So is the investment of the principal. The children have a graduated right to the distribution of the corpus of the trust, one-fourth upon reaching the age of 25, one-fourth at 30, and the balance at 35. Almost simultaneously with the creation of the two trusts a partnership in

the shoe business was entered into effective September 20, 1943, consisting of the members of the family. Jack Smith was assigned 40 per cent, Rose Mae Smith 30 per cent and the Trusts 15 per cent each in the Boston Shoe Company. The wife acquired her interest by surrendering a $60,000.00 note executed to her by Jack Smith. Both trusts exchanged their assets for the respective interests in the new partnership. Under the terms of the partnership, which was modified at one time by including an employee, then returned to the original state, control continued to be exercised by Jack Smith. Salaries of $25,000.00 per year for the husband and $2400.00 for the wife were provided for (Art. V). The net proceeds of the business were to be distributed in accordance with the percentages established by the Trusts. The main partners retained the power to determine the amount of the salaries to be paid to themselves. The salaries were to be paid before any "distributive net profits" and were to be considered a part of the costs of "doing business". No business transaction could be conducted by the partnership without the approval of the husband (Art. VII). Nor could it enter into any contracts or incur any liabilities during the life of the husband, while he was a partner, without his consent. The life of the partnership was set at three years, and thereafter for successive minimum terms of two years. And the husband was given the right to purchase the partnership at book [16] value, in which event no good will could be considered as a part of the same (Art. X, especially

subdivision e). No amendment of the partnership could be made without the consent of the husband. The parents, as the trustees for the children, represented them in the partnership, so that the children had no direct or independent voice in the partnership.

The criteria by which the validity or invalidity of partnerships of this character are determined have been set forth by the Supreme Court in Commissioner vs. Culbertson, 1949, 337 U.S. 733, 742. They have been applied by me on repeated occasions. See, Toor vs. Westover, 1950 D.C. Cal., 94 F. Supp. 860; Schlobohm vs. United States, 1952, D.C. Cal., 105 F. Supp. 593. Among late cases from our Court of Appeals are Parker vs. Westover, 1950, 9 Cir., 186 F(2) 49; Harkness vs. Commissioner, 1952, 9 Cir., 193 F(2) 655. And see, Schallerer vs. Commissioner, 1953, 7 Cir., 203 F(2) 100.

Since the Culbertson case, the fact that the capital which created the trust came from the parents is not determinative of the matter. Courts take the view that the creation of trusts by parents out of concern for the future welfare of the children is a natural and laudable impulse. As said in Miller vs. Commissioner, 1953, 6 Cir., 203 F(2) 350, 354:

> "Human experience teaches that the concern of parents over the financial security of their children is often greater than concern for their own security and enjoyment of the fruits of their labors."

However, the other elements which are spelled out in the [17] Culbertson and subsequent cases, such as (1) absence of change of control in the business, (2) the power to terminate the partnership interest upon the terms of the managing partner, (3) the absence of judicial control through a court-controlled trustee or through a guardianship of the estate of the minors, (4) the lack of any expectation that the children would ever go into the business (a contrary expectation was the primary consideration in the determination of the case of Miller vs. Commissioner, supra, upon which so much reliance is placed by plaintiffs), (5) the large salary voted himself by the father,—$25,000.00, and (6) the unlimited control of both the trusts and partnership,—all these clearly indicate that the partnership had no existence as a taxable entity. In reality, the husband continued to dominate and manage the business as he had before, subject only to the rights of the wife under the community property laws of California (Cal. Civil Code, Secs. 172-172a). That the parents generously deposited the profits of the partnership to the trusts and did not draw from them even legitimate moneys for the education of the children so that, in 1948, the value of each trust was around $115,000.00, is praiseworthy. But the fact remains that the earnings for the years in question were the earnings of "the husband and wife" partnership to which neither the capital, skill or even the future expectations of the children added aught. The Commissioner was, therefore, right in disregarding the partnership of

the children for tax purposes during the years 1943 to 1946.

Hence the ruling above made.

Dated this 24th day of June, 1954.

/s/ LEON R. YANKWICH,
Judge [18]

[Endorsed]: Filed June 24, 1954.

[Title of District Court and Cause.]

FINDINGS OF FACT AND CONCLUSIONS OF LAW

The above case came on regularly for trial on June 18, 1954, before the Honorable Leon R. Yankwich, United States District Judge, sitting without a jury, the plaintiffs, appearing through their counsel, Latham & Watkins, by Henry C. Diehl and Richard W. Lund, Esqs., and the defendants appearing through their counsel, Laughlin E. Waters, United States Attorney for the Southern District of California, Edward R. McHale, Assistant United States Attorney for said District, Chief, Tax Division, and Bruce I. Hochman, Assistant United States Attorney for said District, and evidence both oral and documentary having been received, the Court having duly considered the same and on June 24, 1954, having filed its order of Findings of Fact and Judgment, the Court now finds as follows:

Findings of Fact

I.

Plaintiffs, husband and wife, are both adult citizens of the United States residents of the State of California suing in his or her own right. [19]

II.

Defendant Harry C. Westover was, from July 1, 1943 to October 31, 1949, Collector of Internal Revenue for the Sixth District of California. Defendant Robert A. Riddell was Acting Collector from October 1, 1949 to April 30, 1950, Collector from May 1, 1950 to November 26, 1952, and since said last date, Director of Internal Revenue, all for said Sixth District of California.

III.

In each of his separate Federal income tax returns for the calendar years 1943 to 1946, inclusive, plaintiff Jack Smith reported as income half of his said salary drawings, half of his wife's said salary drawings, and the balance of his distributable share of partnership net income as computed.

IV.

In each of her separate Federal income tax returns for the calendar years 1943 to 1946, inclusive, plaintiff Rose Mae Smith reported as income half of her said salary drawings, half of her husband's said salary drawings, and the balance of her distributable share of partnership net income as computed.

V.

Trusts were formed for the benefit of two minor children, which the Commissioner of Internal Revenue refused to recognize as partners and determined that the partnership income so reported by the two trusts should be taxed half to plaintiff Jack Smith and half to plaintiff Rose Mae Smith. Deficiencies in Federal income tax were assessed against them in accordance with such determination.

VI.

Deficiencies of tax and interest assessed were paid by plaintiffs to defendant Harry C. Westover for the calendar years and in the amounts as follows:

Calendar Year	Plaintiff Jack Smith	Plaintiff Rose Mae Smith
1943	$ 7,803.23	$ 1,463.27
1944	13,664.16	11,961.54
1945	13,355.14	12,748.92
1946	23,907.98	22,565.80

VII.

Plaintiff Jack Smith and plaintiff Rose Smith in their separate Federal income tax returns for the calendar year 1947 reported as income half of their salary allowances, half of each other's salary allowance, their distributable share of partnership net income as computed, and also half for each of the distributable partnership income of the two trusts.

VIII.

In their joint Federal income tax return for the calendar year 1948, plaintiffs reported as income their said salary allowances and their distributable shares of partnership net income as computed and also the distributable partnership income of the two trusts.

IX.

Plaintiffs' Federal income tax returns for the calendar years 1947 and 1948 were filed with, and the taxes shown thereon to be due were paid to, defendant Harry C. Westover. A deficiency of tax and interest in the amount of $2,955.17 for the calendar year 1948 was paid by plaintiffs to defendant Robert A. Riddell. All of the amounts were paid to defendant Harry C. Westover except the amount of $2,955.17 for the calendar year 1948 which was paid to defendant Robert A. Riddell.

X.

Plaintiffs duly filed their respective claims for refund on Treasury Department Form 843 for the calendar years 1943 and 1944 on or about July 19, 1949; for the calendar years 1945 and 1946, on or about May 2, 1950; for the calendar year 1947, on or about March 15, 1951; and for the calendar year 1948 on or about March 15, 1952. In each claim, the reason given in support thereof was that the trusts should be recognized as partners and their shares of the partnership income should be taxed as said trusts rather than to the plaintiffs.

XI.

The Commissioner of Internal Revenue, by registered mail, on or about February 13, 1951, formally rejected said claims for the calendar year 1943, 1944 and 1945, and on or about March 15, 1951, formally rejected said claims for the calendar year 1946. Said claims for calendar years 1947 and 1948 have not yet [21] been formally acted upon, but more than six months elapsed between the filing thereof and the filing of this action.

XII.

The claim arises out of a family partnership in the wholesale shoe business known as the Boston Shoe Company, successfully established by the plaintiff Jack Smith before his marriage to the plaintiff Rose Mae Smith.

XIII.

After marriage the spouses considered that the business was community property to which the husband's earning capacity contributed. On December 31, 1942, the husband bought out the wife's interest for the sum of $102,933.89, the purchase price being represented by four promissory notes in different amounts with different due dates, one year apart, given by him to his wife on the same date.

XIV.

On September 29, 1943, two trusts were created by written instruments for the benefit of the children of Jack and Rose Mae Smith, one designated

as the "Howard Samuel Smith trust", in favor of the son then aged 11; the other named the "Barbara Ann Smith trust", in favor of the daughter then aged 3. The daughter is still underage. The son is now 22, and, after securing a degree in chemistry at Stanford University, entered Harvard University as a post-graduate student, and now has been accepted at the Harvard Law School. Although the son may, during his vacations, have worked in the shoe business, he is not preparing for the business and it is not likely that a man with such educational background would engage in such business with his father after completing his education.

XV.

The corpus of the "Howard Samuel Smith trust" was three United States certificate of indebtedness totaling the principal sum of $30,000.00, given by the father, Jack Smith. The corpus of the "Barbara Ann Smith trust" was a $30,000.00 note executed by plaintiff Jack Smith to his wife Rose Mae Smith on December 31, 1942, and thereafter assigned to the trust by her. [22]

XVI.

The trusts are irrevocable. They are subject to the absolute power of the parents as trustees, the beneficiary having only "the right to enforce" performance. The distribution of the income is controlled by the trustee. So is the investment of the principal. The children have a graduated right to the distribution of the corpus of the trust, one-

fourth upon reaching the age of 25, one-fourth at 30, and the balance at 35.

XVII.

Almost simultaneously with the creation of the two trusts the partnership in the shoe business was entered into effective September 30, 1943, consisting of the members of the family. Jack Smith was assigned 40%; Rose Mae Smith, 30%; and the trust, 15% each in the Boston Shoe Company. The wife acquired her interest by surrendering a $60,000 note executed to her by Jack Smith. Both trusts exchanged their assets for their respective interests in the new partnership.

XVIII.

Under the terms of the partnership, which was modified at one time by including an employee, then returned to the original state, control continued to be exercised by Jack Smith.

XIX.

Salaries of $25,000.00 per year for the husband and $2,400.00 for the wife were provided for under Article 5 of the first partnership agreement and thereafter continued under the other arrangements. The net proceeds of the business were to be distributed in accordance with the percentages established by the trusts.

XX.

The main partners, the two plaintiffs here, retained the power to determine the amount of the

salary to be paid to themselves. The salaries were to be paid before any "distributive net profits" and were to be considered part of the cost of "doing business". [23]

XXI.

No business transaction could be conducted by the partnership without the approval of the husband. Nor could it enter into any contract or incur any liability during the life of the husband, while he was a partner, without his consent.

XXII.

The life of the partnership was set at three years, and thereafter for successive minimum terms of two years.

XXIII.

The husband, plaintiff Jack Smith, was given the right to purchase the partnership at book value, in which event no good will could be considered as part of the same.

XXIV.

No amendment of the partnership could be made without the consent of the husband Jack Smith.

XXV.

The parents, Jack and Rose Mae Smith, as the trustees for the children, represented them in the partnership, so that the children had no direct or independent voice in the partnership.

XXVI.

At all times throughout the years involved con-

trol was exercised and maintained by the plaintiffs in this action. The creation of the partnership and trusts effected no change in the control of the business. The children had no independent voice in the management of the business either personally or through the trusts.

XXVII.

The power to terminate the partnership interest remained upon the terms of the managing partner, namely, Jack Smith.

XXVIII.

There was no judicial control of the children's interests through a court controlled trustee or through a guardianship of the estate of the minors.

XXIX.

There was a lack of any expectation that the children would ever go into the business.

XXX.

The father, plaintiff Jack Smith, voted a very large salary to himself, namely, $25,000.00.

XXXI.

The plaintiffs retained unlimited control of both the trust and the partnership, indicating clearly that the partnership had no existence as a taxable entity.

XXXII.

The children through the trust or otherwise added neither fresh capital nor skill nor even the future expectation of services.

Conclusions of Law

I.

This Court has jurisdiction of this controversy and of the parties hereto.

II.

The partnerships, entered into between the trusts and the plaintiffs Jack Smith and Rose Mae Smith and later Herman Weishaupt, have no validity for income tax purposes for the years 1943 to 1948, inclusive.

III.

Neither children nor trusts for children either intended to or did enter into a bona fide partnership with their parents for a business purpose.

IV.

The Commissioner was, therefore, right in disregarding the partnership of the children for tax purposes during the years 1943 to 1946 to 1948.

V.

Plaintiffs have failed to sustain their burden of proof of showing defendants erroneously assessed and collected taxes from the plaintiffs. [25]

VI.

Defendants are entitled to judgment. Plaintiffs take nothing by this action and the complaint is

dismissed with prejudice and with costs to the defendants.

Dated: This 23rd day of August, 1954.

/s/ LEON R. YANKWICH,
United States District Judge [26]

[Endorsed]: Lodged Aug. 6, 1954. Filed Aug. 23, 1954.

In the United States District Court of the Southern District of California, Central Division

No. 15161-Y Civil

JACK SMITH and ROSE MAE SMITH,
Plaintiffs,

vs.

HARRY C. WESTOVER, former Collector of Internal Revenue, and ROBERT A. RIDDELL, Director of Internal Revenue,
Defendants.

JUDGMENT

The above cause came on regularly for trial on June 18, 1954, before the Honorable Leon R. Yankwich, United States District Judge, sitting without a jury, the plaintiffs appearing through their counsel, Latham & Watkins by Henry C. Diehl and Richard W. Lund, Esqs., and the defendants appearing through their counsel Laughlin E. Waters, United States Attorney for the Southern District

of California, Edward R. McHale, Assistant United States Attorney for said District, Chief, Tax Division, by Bruce I. Hochman, Assistant United States Attorney for said District, and evidence both oral and documentary having been received, the Court having after due deliberation on June 24, 1954, rendered its order for findings of fact and judgment and having filed its [27] Findings of Fact and Conclusions of Law and ordered that judgment be entered in favor of the defendants in accordance with said findings and conclusions;

Now, Therefore, It Is Hereby Ordered, Adjudged and Decreed that the plaintiffs' complaint and prayer for judgment be denied and that the plaintiffs take nothing by reason of this action and that defendants have judgment for and shall recover from plaintiffs the amount of defendants' costs to be taxed by the Clerk of this Court in the sum of $20.00.

Judgment rendered this 23rd day of August, 1954.

/s/ LEON R. YANKWICH,
United States District Judge [28]

Affidavit of Service by Mail attached. [29]

[Endorsed]: Lodged Aug. 6, 1954. Judgment Docketed and Entered Aug. 23, 1954. Filed Aug. 23, 1954.

[Title of District Court and Cause.]

PLAINTIFFS' MOTIONS TO AMEND FINDINGS AND JUDGMENT AND FOR A NEW TRIAL

Plaintiffs, by Latham & Watkins, their attorneys herein, respectfully move that the Court:

(1) Amend its findings, make additional findings, and amend the judgment accordingly, as hereinafter set forth, pursuant to rule 52 of the FRCP.

(2) Grant a new trial, open the judgment, amend and make new findings of fact, make new conclusions, and direct entry of a new judgment, as hereinafter set forth, pursuant to rule 59 of the FRCP.

The grounds upon which plaintiffs rely are that the Court erred in both fact and law. The motions are based upon the entire record, to which appropriate references will be made in the detailed specifications of error which follow. [30]

Errors

I.

The Court erred in finding (Para. XIII of Findings of Fact) that the spouses considered that the business was community property. Only part, in the total amount of $205,867.79, was so considered. (Exh. 2; Tr. 49.)

II.

The Court erred in finding (Para. XIV) that plaintiffs' son is not preparing for the business and that it is not likely that a man with such educa-

tional background would engage in such business with his father after completing his education. There is no evidence in the record from which such a finding can be made by inference or otherwise.

III.

The Court erred in finding (Para. XVI) that the trusts are subject to the absolute power of the parents as trustees and that the distribution of the income and the investment of principal is controlled by the trustees. The parents are subject to the usual obligations of fiduciaries and the children as beneficiaries are entitled to faithful performance of the trusts. The trustees are required to accumulate trust income, except for payment of trust administration expenses. The trustees have no discretion respecting distributions to beneficiaries until after the beneficiaries reach the age of 21 years, at and after which time limited amounts may be distributed. Final distributions of corpus and accumulated income are specified by the trust instruments. (Exhs. 7 and 8, Article III (c) and (d) of each.) As a matter of fact, all living expenses of the children have been paid by the parents.

IV.

The Court erred in finding (Para. XVIII) that control of the partnership continued to be exercised by Jack Smith. In all events, any control was subject to the limitations of the partnership [31] agreements. (Exhs. 13 and 15.) Particularly in the partnership effective from January 1, 1945 to June 30,

1948, Jack Smith had no powers not also resting in other partners and he did not own a controlling interest. Individually he owned a 36% interest and as trustee he held a 13½% interest, totalling only 49½%. (Exh. 15.)

V.

The Court erred in finding (Para. XX) that the plaintiffs retained the power to determine the amount of salary to be paid themselves. Under both partnership agreements, salaries were to be determined by the partners and under the second agreement, neither plaintiff owned a controlling interest.

VI.

The Court erred in finding (Para. XXI) that the partnership could not conduct any business transaction, enter into any contract, or incur any liability without the husband's consent. There was no such provision in the agreement effective from January 1, 1945 to June 30, 1948 (Exh. 15) and he in fact did not have control of that partnership.

VII.

The Court erred in finding (Para. XXII) that the life of the partnership was set at three years and thereafter for successive minimum terms of two years. The first partnership (Exh. 13) was to run for twenty years (Article IX).

VIII.

The Court erred in finding (Para. XXIII) that the plaintiff Jack Smith was given the right to pur-

chase the partnership at book value without also finding that all partners had the same right and that such right arose only as to the interest of a withdrawing or deceased partner. (Exhs. 13 and 15.)

IX.

The Court erred in finding (Para. XXIV) that no amendment of the partnership could be made without the consent of Jack Smith. [32] The second partnership (Exh. 15) specifically lodged said right in the partners entitled to receive a majority of the profits (Article XIII) and Jack Smith was not so entitled.

X.

The Court erred in finding (Para. XXVI) that creation of the partnership and trusts effected no change in the control of the business. Prior to the formation of the first partnership, Jack Smith owned and controlled 100% of the business. (Exh. 2.) During the first partnership, from October 1, 1943 to December 31, 1944, he owned but 40% individually and 15% as trustee, while Rose Mae Smith owned 30% individually and 15% as trustee. (Exh. 13.) During the second partnership, from January 1, 1945 to June 30, 1948, the interests were further changed to 36% for Jack Smith individually and 13½% as trustee, 27% for Rose Mae Smith individually and 13½% as trustee, and 10% for Herman Weishaupt, in no way related to any of the Smiths. (Exh. 15.) Furthermore, there is a basic difference between control exercised with unlimited discretion solely for one's personal benefit

and control exercised in a fiduciary capacity as a partner.

XI.

The Court erred in finding (Para. XXVII) that the power to terminate the partnership interest remained upon the terms of Jack Smith. There is nowhere in the record any evidence to support such a finding or from which such a finding might be inferred. A termination by him would constitute him a withdrawing partner and give the other partners the right to purchase his interest at book value. (Exhs. 13 and 15.)

XII.

The Court erred in finding (Para. XXVIII) that there was no judicial control of the children's interests through a court controlled trustee. While no intervivos trust is under court supervision in the sense that periodic reports are required, all [33] trustees are subject to court control.

XIII.

The Court erred in finding (Para. XXIX) that there was a lack of any expectation that the children would ever go into the business. Not only is there nothing in the record to support such a finding, but plaintiff Jack Smith testified that he hoped and expected that his son would go into the business. (Tr. 52-53.)

XIV.

The Court erred in finding (Para. XXX) that plaintiff Jack Smith voted a very large salary to

himself. The salary was determined by the partners in accordance with the partnership agreements and not by the "vote" of Jack Smith. The record shows that the amount was reasonable for the services rendered and the Court further erred in not so finding.

XV.

The Court erred in finding (Para. XXXI) that the plaintiffs retained unlimited control of both the trust and the partnership, indicating clearly that the partnership had no existence as a taxable entity. As already set forth, neither in fact nor law did the plaintiffs have unlimited control.

XVI.

The Court erred in finding (Para. XXXII) that the children through the trusts or otherwise added neither fresh capital nor skill nor even the future expectation of services. The trusts each contributed $30,000.00 of capital of which they were the owners. The trustees participated in the operation of the business. As already shown, there was an expectation of services by the son.

XVII.

The Court erred in failing to make the following findings of fact:

(1) That capital was an important income producing element in the business of the Boston Shoe Co. [34]

(2) That the purpose of the trusts was to create an estate for said children upon their maturity.

(3) That the parents had planned first to invest the initial trust corpus in real estate and had abandoned this plan because of the inflated condition of real estate, and had invested said moneys in the shoe business in the belief that said business afforded the best opportunity to create a sizeable estate for the children.

(4) That the parents explained to their children the extent of the interest of each in the partnership.

(5) That fictitious name certificates were filed.

(6) That copies of the trust agreements and the partnership agreements were filed with the Union Bank as successor trustee.

(7) That under the trust agreements the trustees did not and could not use any part of income or principal to satisfy the trustees' legal obligations to support their children or for any other purpose benefiting the plaintiffs.

(8) That the parents deposited the trusts' shares of partnership income in trust bank accounts and did not draw from them even legitimate moneys for the education of the children so that, in 1948, the value of each trust was approximately $115,000.00.

(9) That the trust funds were managed by plaintiffs as fiduciaries, and that they at all times fulfilled their obligations as such fiduciaries.

(10) That Jack Smith's salary allowance of $25,000.00 per year was reasonable in amount for the services rendered.

(11) That Rose Mae Smith worked in the busi-

ness and that her salary allowance of $2,400.00 per year was reasonable in amount for the services rendered.

(12) That the trusts were valid legal entities entitled [35] to full recognition.

(13) That the partnerships were valid partnerships entitled to recognition for tax purposes.

(14) That the trusts' shares of the partnership income were taxable to the trusts and not the plaintiffs.

Points and Authorities

There is a basic difference between control exercised with unlimited discretion solely for one's personal benefit and control exercised only in a fiduciary capacity as a partner.

Toor vs. Westover, 200 F.2d 713 at 715.

Although the Toor case, supra, involved a limited partnership and the fiduciary relationship of a general partner to the limited partners, the same relationship exists between partners in a general partnership.

Sec. 15021, Calif. Corp. Code.
McMillen vs. Olmstead, 85 Cal. App. 656.
Perelli-Minetti vs. Lawson, 205 Cal. 642.

Although Congress has specifically provided that determinations as to the validity of a family partnership for tax purposes for any taxable year beginning before January 1, 1951 as if section 340(b) of the Revenue Act of 1951 had not been enacted, it is proper to refer to the legislative history of that

new statute in seeking to arrive at the prior status of the law.

Toor vs. Westover, 200 F.2d 713 at 716.

Two principles governing attribution of income have long been accepted as basic: (1) income from property is attributable to the owner of the property; (2) income from personal services is attributable to the person rendering the services. There is no reason for applying different principles to partnership income. If an individual makes a bona fide gift of real estate, or of a share of corporate stock, the rent or dividend income is taxable to the donee. Your committee's amendment makes it clear that, however [36] the owner of a partnership interest may have acquired such interest, the income is taxable to the owner, if he is the real owner. If the ownership is real, it does not matter what motivated the transfer to him or whether the business benefited from the entrance of the new partner.

Substantial powers may be retained by the transferor as a managing partner or in any other fiduciary capacity which, when considered in the light of all the circumstances, will not indicate any lack of true ownership in the transferee. In weighing the effect of a retention of any power upon the bona fides of a purported gift or sale, a power exercisable for the benefit of others must be distinguished from a power vested in the transferor for his own benefit.

H. R. Rep. No. 586, 82nd Cong., 1st Sess., Sec. V. M.

Sen. Rep. No. 781, 82nd Cong., 1st Sess., Sec. VI A 7.

1951-2 Cumulative Bulletin 380 and 485.

The Court ignored the trusts and treated them as having no legal existence, apparently only because the parents, rather than some other persons, were trustees. No authority has been found for such a determination. The parents, as trustees, had no powers different from those which a so-called independent trustee would have had. In fact, provision was made for successor trustees with the same powers.

This Court (Judge Yankwich) has upheld a family partnership under circumstances similar to those in this case, except that the children's uncle was trustee. He was no more "independent" nor subject to court supervision than are the parents here.

Osbrink vs. U. S., . . Fed. Supp. . . (1952).

This Court (Judge Harrison) has also upheld a family partnership where one parent-partner held the minor's interest as guardian.

Flandrick vs. U. S., 99 F. Supp. 718. [37]

At least one case has upheld a family partnership where the parents were trustees for the children.

Miller vs. Commissioner, 203 F.2d 350.

Referring further to the Miller case, supra, we respectfully disagree with this Court that an expectation that the children would go into the business "was the primary consideration in the determination of the case." (Memorandum Decision, p. 5.) The Court stated that the fact that the children were attending a pharmacy college "may indicate

that the inducement of giving them an interest in the business has stimulated them to study and prepare themselves in this field of endeavor." (Underscoring supplied.) In other words, the trusts and partnership were established to induce the children to go into the business. It was not the expectation that they would that induced the parents to establish the trusts and partnership.

The same inducement was present in the case at hand when the trusts and partnership were established in 1943. The fact that the children are not yet in the business does not detract from the original purpose.

The basis for the Miller decision was that the trusts were set up for the benefit of the children, for their financial security, to give them an interest in the business and an incentive to engage therein. Every one of those elements is present in the case at hand.

Plaintiffs did not have unlimited control over the trusts, because control is exercised by courts of equity to which the beneficiaries could resort. Furthermore, the record shows that the trustees were most conscientious in the performance of their fiduciary obligations.

Miller vs. Commissioner, 203 F.2d 350 at 352.

The Court has referred to "the large salary voted himself by the father,—$25,000.00," as a point against the plaintiffs. [38] Adequate compensation for working partners has always been a requirement for the recognition of family partnerships. Not to provide a substantial salary for Jack Smith

would allocate to the trusts more than their proper share of partnership income and would indicate a lack of reality in the partnership. The salary allowance should be and is a point in plaintiffs' favor.

In the Revenue Act of 1951, referred to above, Congress made sure that such salaries would be provided by making it a specific requirement of the law.

Conclusion

For the reasons stated, it is respectfully submitted that the Court should open the judgment, amend its findings in conformity herewith, and direct entry of judgment in favor of the plaintiffs.

September 1, 1954.

LATHAM & WATKINS,
/s/ By HENRY C. DIEHL,
Attorneys for Plaintiffs [39]

Acknowledgment of Service attached. [40]

[Endorsed]: Filed September 2, 1954.

[Title of District Court and Cause.]

MINUTES OF THE COURT

Date: Sept. 13, 1954. At Los Angeles, Calif.

Present: Hon. Leon R. Yankwich, District Judge. Deputy Clerk: John A. Childress, Reporter: Marie Zellner.

Counsel for Plaintiffs: Henry C. Diehl.

Counsel for Defendants: Bruce I. Hochman.

Proceedings: For hearing motions of plaintiffs, filed Sept. 2, 1954, (1) to amend findings and judgment; and (2) for new trial.

It is Ordered that said motions are denied.

EDMUND L. SMITH,
Clerk
/s/ By JOHN A. CHILDRESS,
Deputy Clerk [41]

[Title of District Court and Cause.]

NOTICE OF APPEAL

Notice Is Hereby Given that Jack Smith and Rose Mae Smith, plaintiffs above named, hereby appeal to the United States Court of Appeals for the Ninth Circuit from the final judgment entered in this action on August 23, 1954.

Dated: November 2, 1954.

LATHAM & WATKINS,
/s/ By HENRY C. DIEHL,
Attorneys for Appellants Jack Smith and Rose Mae Smith [42]

Affidavit of Service by Mail attached. [43]

[Endorsed]: Filed November 3, 1954.

[Title of District Court and Cause.]

DESIGNATION OF RECORD

To the Clerk of the United States District Court for the Southern District of California, Central Division:

Pursuant to Rule 75(a) of the Federal Rules of Civil Procedure, appellants designate the following portions of the record to be contained in the record on appeal in the above-entitled action to the Circuit Court of Appeals for the Ninth Circuit:

1. Complaint.

2. Answer.

3. Stipulation (of facts).

4. Transcript of evidence and proceedings on the trial.

5. Plaintiffs' exhibits.

6. Memorandum decision.

7. Findings of Fact and Conclusions of Law.

8. Judgment. [44]

9. Plaintiffs' Motions to Amend Findings and Judgment and for a New Trial.

10. Order Denying Motions to Amend and for a New Trial.

11. Notice of Appeal, with date of filing.

12. This designation.

Dated: November 2, 1954.

LATHAM & WATKINS,
/s/ By HENRY C. DIEHL,
Attorneys for Appellants Jack Smith and Rose Mae Smith [45]

Affidavit of Service by Mail attached. [46]

[Endorsed]: Filed November 3, 1954.

[Title of District Court and Cause.]

CERTIFICATE OF CLERK

I, Edmund L. Smith, Clerk of the United States District Court for the Southern District of California, do hereby certify that the foregoing pages numbered from 1 to 46, inclusive, contain the original Complaint; Answer; Memorandum Decision; Findings of Fact and Conclusions of Law; Judgment; Motions to Amend Findings of Fact and Judgment and for New Trial; Notice of Appeal and Designation of Record on Appeal and a full, true and correct copy of the Minutes of the Court for September 13, 1954, which, together with original plaintiff's exhibits 1 to 22, inclusive, and reporter's transcript of proceedings on June 18, 1954, transmitted herewith, constitute the transcript of record on appeal to the United States Court of Appeals for the Ninth Circuit.

I further certify that my fees for preparing and certifying the foregoing record amount to $2.00 which sum has been paid to me by appellants.

Witness my hand and the seal of said District Court this 8th day of December, A. D. 1954.

[Seal] EDMUND L. SMITH,
Clerk
/s/ By THEODORE HOCKE,
Chief Deputy

In the United States District Court for the Southern District of California, Central Division

No. 15,161-Y Civil

JACK SMITH and ROSE MAE SMITH,
Plaintiffs,

vs.

HARRY C. WESTOVER, former Collector of Internal Revenue, and ROBERT A. RIDDELL, Director of Internal Revenue,
Defendants.

TRANSCRIPT OF PROCEEDINGS

Los Angeles, Calif., Friday, June 18, 1954

Honorable Leon R. Yankwich, Judge presiding.

Appearances: For the Plaintiffs: Latham & Watkins, by Richard W. Lund and Henry C. Diehl, 900 Wilshire Blvd., Suite 830, Los Angeles 17, Calif.

For the Defendants: Laughlin E. Waters, United States Attorney, by Bruce I. Hochman, Assistant United States Attorney. [1*]

The Clerk: No. 15,161, Jack Smith and Rose Mae Smith vs. Harry C. Westover, et al., for trial. Mr. Diehl and Mr. Lund are present for the plaintiffs, and Mr. Bruce I. Hochman for the defendants.

The Court: Do you desire to make an opening statement? You filed a trial memorandum that seems to set forth the essentials of the controversy.

The Clerk: Mr. Diehl speaking.

Mr. Diehl: Your Honor, this, as you know, is a family partnership case.

The Court: That is right.

Mr. Diehl: The background is this, which the evidence will show: Mr. and Mrs. Smith, the plaintiffs, husband and wife, were married in 1931.

The Court: Just a moment.

Mr. Diehl: (Continuing) From that time until October 1, 1943, the business of the Boston Shoe Company was operated as an individual proprietorship of the plaintiff, Jack Smith.

At December 31, 1942, the plaintiffs, Jack and Rose Mae Smith, entered into an agreement by which the community interests of Rose Mae Smith in the business was purchased by her husband, Jack Smith.

Thereafter, in connection with their over-all planning, [2] and their desire to provide an estate for

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* Page numbers appearing at top of page of original Reporter's Transcript of Record.

their children, plans were made to set up trusts for the children, to which each of the parents would contribute the maximum allowed under the gift tax law tax-free, to wit, $30,000.00.

At first it was thought that the trust funds might be invested in real estate. By the time the trusts were actually set up or in condition to be set up, it was their opinion that the real estate market had risen too much, and that that would not be a good investment.

They, therefore, decided to put the trusts into the partnership, which was the business best known by the husband, and which he considered he could use to the best advantage for the benefit of the children's trust.

Accordingly, the trusts were established on September 29, 1943.

The plaintiff, Jack Smith, contributed to his wife as trustee for his son three government bonds totaling $30,000.00.

The plaintiff, Rose Mae Smith, contributed to her husband, as trustee for the daughter, one of the notes for $30,000.00 which she had received from her husband in connection with the 1942 transaction, by which he had acquired her community interest.

At the same time the plaintiff, Rose Mae, repurchased an interest in the business to the extent of 30 per cent with two other of the $30,000.00 notes which she had received from [3] her husband.

Then each trust purchased from the husband a 15 per cent interest in the business, the one trust using the government bonds in the purchase price,

and the other trust using the note. Thereupon——

The Court: Who were the trustees?

Mr. Diehl: Jack Smith, the plaintiff Jack Smith was trustee for the daughter's trust, and the plaintiff Rose Mae Smith was trustee for the son's trust.

The Court: Was there any action taken making them guardians of the estate, under the state law?

Mr. Diehl: No guardianship; just a trusteeship.

The Court: In other words, these were just one of these paper trusts that could be dissolved whenever they wanted to, and not bound by or controlled by any court.

Mr. Diehl: The trusts were irrevocable.

The Court: I know that, but they were not subject to any control by any court.

Mr. Diehl: Well, only insofar as any trust is subject to control by a court.

The Court: I mean, they were minors,——

Mr. Diehl: That is right.

The Court: ——and they made themselves guardians of the estate by virtue of parenthood without an order of the court?

Mr. Diehl: That is correct. [4]

The Court: I see. All right.

Mr. Diehl: Then on October 1, 1943, the Partnership No. 1 was established by a written agreement, which will be in evidence, by which the plaintiff Jack Smith had a 40 per cent interest, the plaintiff Rose Smith had a 30 per cent interest, and each of the trusts a 15 per cent interest.

The Court: And who represented the children in the partnership,—the parents?

Mr. Diehl: The parents as trustees. The partnership was between the two parents as individuals, and the two parents as trustees.

The Court: All right.

Mr. Diehl: That partnership continued until December 31, 1944, at which time one Herman Weishaupt, who was a key employee of the business, was taken in effective January 1, 1945, and a new partnership agreement was entered into at that time.

Herman Weishaupt acquired a 10 per cent interest, which reduced Jack Smith's interest to 36 per cent, Rose Mae Smith's interest to 27 per cent, and the two trusts to 13½ per cent. That was done by the contribution of additional capital by Weishaupt.

That partnership continued until June 30, 1948, at which time Weishaupt withdrew. His interest was acquired by Jack Smith, and the new partnership of the original four resumed at July 1, 1948.

The third partnership is not involved directly in this action for the reason that it adopted the January 31st fiscal year, so that its first year ended in 1949.

This case involves only the years 1943 through 1948 of the individuals.

Now, the Government, of course, has not questioned the interest of Jack and Rose Mae Smith, as individuals, in the profits of the business.

The Government has denied recognition to the trusts as partners. Deficiencies were proposed and paid by the plaintiffs for the years 1943 to 1946.

Thereupon the plaintiffs adopted a different pro-

cedure than before, and while partnership returns were filed showing the interests of all the partners, the parents under protest reported on their individual returns the income which was allocable to the trusts, and then thereafter filed claims for refund.

Now, in our evidence we propose——

The Court: That is sufficient. We will hear the rest from the witnesses.

Any statement by the Government?

The Clerk: Mr. Bruce Hochman.

Mr. Hochman: May it please the court: The Government contends, your Honor, that it was not a bona fide business purpose that was involved in the partnership trust arrangements, [6] and that the Commissioner is correct in the disallowance for income tax purposes of the arrangements set up by the plaintiffs.

The Court: I have had this type of case before me before, and I have ruled both ways, as shown by the fact that when I ruled in favor of the taxpayer, the Government appealed, and when I ruled against the taxpayer, the taxpayer appealed.

The Schlobohn case was a case in which I did not recognize the partnership, and there was another case—I forget the title of it—where I held the partnership was a valid partnership. So far as I am concerned, no law goes prior to those three decisions of the Supreme Court.

Mr. Hochman: The Tower case, the Culbertson case,——

The Court: ——the Tower case, the Culbertson case, and the third one.

Mr. Hochman: The Lusthaus case.

The Court: No law before that interests me, because no law before that is of any validity, because in those cases the court has laid down the criteria which we have to follow, and the question always is: Are these criteria which make a partnership valid or invalid in the present and particular case?

So let's go ahead and hear the evidence.

Mr. Diehl: If the court please, we have a brief written stipulation of facts, we have a brief oral stipulation to make, [7] and then we have numerous documents which counsel have agreed may go into evidence without further identification.

The Court: All right.

Mr. Diehl: I would offer, first, the written stipulation of facts, which in effect reduces the issues to the one question of whether the partnership was valid, and which also recites the fact that fictitious name certificates were filed by the two partnerships that were mentioned.

The Court: All right. It may be received.

The Clerk: Plaintiffs' Exhibit 1 in evidence.

(The document referred to was marked Plaintiffs' Exhibit 1 and was received in evidence.)

[See page 162.]

Mr. Diehl: Now, the oral stipulation I can take up next, before the documents.

The Court: All right.

Mr. Diehl: In the Complaint it is alleged, and denied on lack of information, that for the years 1943 to 1946, inclusive, the parents and the two

trusts filed returns reporting their shares of the partnership income, in accordance with their agreement, and paying their respective taxes.

The Court: All right.

Mr. Diehl: For the years 1947 and 1948 the partnership return reflects the income referred to in the agreement, but the parents reported all the partnership income under protest.

The trusts filed their own returns, which included only [8] other income, such as interest,—I guess interest was all in the bank account.

The Court: All right.

Mr. Diehl: Now, I believe it is agreeable to the defendant at this time to stipulate that that is the fact.

Mr. Hochman: So stipulated, your Honor.

The Court: All right.

Mr. Diehl: Now, we offer as Plaintiffs' Exhibit 2 the agreement of purchase by the husband of the community interest of the wife in the specific property, which is the agreement of December 31, 1942, by which the husband purchased the wife's community interest.

The Court: All right.

Mr. Diehl: We have executed copies of all of these documents, but counsel for the Government has agreed that we may introduce copies.

The Court: All right.

The Clerk: Is this admitted, your Honor?

The Court: It may be received.

The Clerk: Plaintiffs' 2 in evidence.

(The document referred to was marked Plaintiffs' Exhibit 2 and was received in evidence.)

[See page 164.]

Mr. Diehl: Plaintiffs' Exhibits 3, 4, 5 and 6 are promissory notes. I should take them up one at a time.

Plaintiffs' 3, note dated December 31, 1942, payable [9] to Rose Mae Smith by Jack Smith for $30,000.00, due in one year. On the back it is endorsed, "Pay to the order of Jack Smith, Rose Mae Smith."

The Court: All right.

The Clerk: Plaintiffs' 3 in evidence.

(The document referred to was marked Plaintiffs' Exhibit 3 and was received in evidence.)

[See page 169.]

Mr. Diehl: Plaintiffs' 4 is also a $30,000.00 note from the same payor to the same payee, of the same date, due in two years. It is endorsed on the back, "Payable to the order of Jack Smith. Rose Mae Smith."

The Clerk: Is this admitted, your Honor?

The Court: It may be received.

The Clerk: Plaintiffs' 4 in evidence.

(The document referred to was marked Plaintiffs' Exhibit 4 and was received in evidence.)

[See page 170.]

Mr. Diehl: As Plaintiffs' 5, a third $30,000.00 note, the same parties, the same date, due in three

years, endorsed on the back, "Pay to the order of Jack Smith as Original Trustee of the Barbara Ann Smith Trust, a Voluntary Express Trust. Rose Mae Smith." Also a typewritten endorsement, "Pay to the order of Jack Smith, individually, in pursuance to agreement of sale and purchase of undivided interest in property."

The Clerk: Is this admitted, your Honor? [10]

The Court: It may be received.

The Clerk: Plaintiffs' 5 in evidence.

(The document referred to was marked Plaintiffs' Exhibit 5 and was received in evidence.)

[See page 170.]

Mr. Diehl: As Plaintiffs' 6, a note of the same date, between the same parties, but in the amount of $12,933.89, due in four years.

The Clerk: Is this admitted, your Honor?

The Court: It may be received.

The Clerk: Plaintiffs' 6 in evidence.

(The document referred to was marked Plaintiffs' Exhibit 6 and was received in evidence.)

[See page 171.]

Mr. Diehl: Exhibit 7, declaration of trust by Jack Smith, original trustee, and Rose Mae Smith, trustor, for the benefit of the daughter Barbara Ann Smith.

The Court: What were the ages of the children at the time?

Mr. Diehl: Nine and two, I believe.

Mr. Jack Smith: Howard was born in '32, so in

1942 he was 11, and Barbara was born in 1940, so she was three.

Mr. Diehl: Eleven years old for the son, and three years old for the daughter.

The Clerk: Is this admitted, your Honor?

The Court: It may be received.

The Clerk: Plaintiffs' 7 in evidence. [11]

(The document referred to was marked Plaintiffs' Exhibit 7 and was received in evidence.)

[See page 171.]

Mr. Diehl: Plaintiffs' Exhibit 8 is a declaration of trust between Rose Mae Smith, original trustee, and Jack Smith, trustor, for the benefit of the son, Howard Samuel Smith.

Both trust declarations are dated September 29, 1943.

The Clerk: Is this admitted, your Honor?

The Court: It may be received.

The Clerk: Plaintiffs' 8 in evidence.

(The document referred to was marked Plaintiffs' Exhibit 8 and was received in evidence.)

[See page 193.]

Mr. Diehl: As Plaintiffs' 9, assignment and transfer by trustor Jack Smith to trustee Rose Mae Smith of three $10,000.00 government bonds, dated September 29, 1943.

The Clerk: Is this admitted, your Honor?

The Court: It may be received.

The Clerk: Plaintiffs' 9 in evidence.

(The document referred to was marked Plaintiffs' Exhibit 9 and was received in evidence.)

[See page 194.]

Mr. Diehl: Plaintiffs' 10, assignment by trustor Rose Mae Smith to trustee Jack Smith of a note in the amount of $30,000.00, dated September 29, 1943.

The Clerk: Is this admitted, your Honor?

The Court: It may be received. [12]

The Clerk: Plaintiffs' 10 in evidence.

(The document referred to was marked Plaintiffs' Exhibit 10 and was received in evidence.)

[See page 195.]

Mr. Diehl: Plaintiffs' 11, agreement of sale and purchase of the interest in specific property, between Jack Smith, seller, and Rose Mae Smith, purchaser, dated September 29, 1943, by which Rose Mae Smith purchased a 30 per cent interest in the Boston Shoe Company, a business.

The Clerk: Is this admitted, your Honor?

The Court: It may be received.

The Clerk: Plaintiffs' 11 in evidence.

(The document referred to was marked Plaintiffs' Exhibit 11 and was received in evidence.)

[See page 196.]

Mr. Diehl: Plaintiffs' 12, agreement of sale and purchase of undivided interest in property, dated September 30, 1943, by which Jack Smith sold to each of the trusts a 15 per cent interest in the

Boston Shoe Company, for a consideration of $30,000.00 from each of them.

The Clerk: Is this admitted, your Honor?

The Court: It may be received.

The Clerk: Plaintiffs' 12 in evidence.

(The document referred to was marked Plaintiffs' Exhibit 12 and was received in evidence.)

[See page 202.]

Mr. Diehl: Plaintiffs' 13, articles of co-partnership, dated October 1, 1943, between Jack Smith and Rose Mae Smith, [13] as individuals, and Jack Smith, as trustee, and Rose Mae Smith, as trustee.

The Clerk: Is this admitted, your Honor?

The Court: It may be received.

The Clerk: Plaintiffs' 13 in evidence.

(The document referred to was marked Plaintiffs' Exhibit 13 and was received in evidence.)

[See page 208.]

Mr. Diehl: Exhibit 14 is a supplement to the articles of co-partnership, Exhibit 13, the supplement bearing the same date, and between the same parties, providing for a salary allowance of $25,000.00 per year to Jack Smith and $2,400.00 a year to Rose Mae Smith.

The Court: It may be received.

The Clerk: Plaintiffs' Exhibit 14 in evidence.

(The document referred to was marked Plaintiffs' Exhibit 14 and was received in evidence.)

[See page 234.]

Mr. Diehl: Plaintiffs' 15, articles of co-partnership, dated January 1, 1945, between Jack Smith and Rose Mae Smith, as individuals, and Jack Smith and Rose Mae Smith, as trustees, and Herman Weishaupt, being the second partnership which was referred to in my opening statement.

The Clerk: Is this admitted, your Honor?

The Court: It may be received.

The Clerk: Plaintiffs' 15 in evidence.

(The document referred to was marked Plaintiffs' Exhibit 15 and was received in evidence.)

[See page 237.]

Mr. Diehl: Plaintiffs' 16 is an agreement dated January 2, 1948, between Jack Smith and Rose Mae Smith, individually, and also as trustees, providing for payment by the trustees of income taxes on the trusts' share of the partnership income, even though charged by the Government to the parents.

The Clerk: Is this admitted, your Honor?

The Court: It may be received.

The Clerk: Plaintiffs' Exhibit 16 in evidence.

(The document referred to was marked Plaintiffs' Exhibit 16 and was received in evidence.)

[See page 268.]

Mr. Diehl: 17 is a schedule entitled, "Boston Shoe Company, Condensed Balance Sheet as of September 30, 1943," which is for the purpose of showing what the books showed on that date as the balance sheet of the individual proprietorship immediately prior to the formation of the partnership.

The Clerk: Is this admitted, your Honor?

The Court: It may be received.

The Clerk: Plaintiffs' 17 in evidence.

(The document referred to was marked Plaintiffs' Exhibit 17 and was received in evidence.)

[See page 272.]

Mr. Diehl: Plaintiffs' 18 is a schedule entitled, "Condensed Balance Sheets of Boston Shoe Company, October 1, 1943, to June 30, 1948," which is for the purpose of showing what the partnership books showed as the balance sheets at the various dates indicated on the schedule. [15]

The Clerk: Is this admitted, your Honor?

The Court: It may be received.

The Clerk: Plaintiffs' 18 in evidence.

(The document referred to was marked Plaintiffs' Exhibit 18 and was received in evidence.)

[See page 273.]

Mr. Diehl: Plaintiffs' 19 is a schedule entitled, "Analysis of Partners' Capital Accounts, Boston Shoe Company, October 1, 1943, to June 30, 1948," for the purpose of reflecting what the books showed as the partners' capital accounts between the two dates mentioned.

The Clerk: Is this admitted, your Honor?

The Court: It may be received.

The Clerk: Plaintiffs' 19 in evidence.

(The document referred to was marked Plaintiffs' Exhibit 19 and was received in evidence.)

[See page 274.]

Mr. Diehl: And Plaintiffs' 20 is a schedule entitled "Analysis of Partners' Drawing Accounts, Boston Shoe Company, October 1, 1943, to June 30, 1948," which schedule reflects what the books showed as to the drawings by the various partners.

The Clerk: Is this admitted, your Honor?

The Court: It may be received.

The Clerk: Plaintiffs' 20 in evidence.

(The document referred to was marked Plaintiffs' Exhibit 20 and was received in evidence.) [16]

[See page 275.]

Mr. Lund: We are ready for our first witness, your Honor, —Mrs. Smith.

The Clerk: Mr. Lund speaking.

The Court: As you know, gentlemen, I have been out of the district, and in addition to being a trial judge, I am also chief judge, and I have all sorts of matters to take care of, and the only time I have is during the recesses, so we will have a short recess.

(A short recess.)

The Court: All right, gentlemen.

Mr. Lund: Mrs. Smith, will you take the stand, please?

ROSE MAE SMITH

called as a witness on behalf of the plaintiffs, having been first duly sworn, was examined and testified as follows:

The Clerk: What is your name, please?

The Witness: Rose Mae Smith.

Direct Examination

Q. (By Mr. Lund): Will you keep your voice up, Mrs. Smith, so that we can hear you back here?

A. Yes, I will.

Q. Your address, please?

A. 2228 North Catalina Street.

Q. You are a plaintiff in this action, together with Mr. Jack Smith? [17]

A. That's right.

Q. And Mr. Jack Smith is your husband?

A. Correct.

Q. In what year were you married?

A. 1931.

Q. How old are you, Mrs. Smith?

A. That's a terrible question to ask me. 46.

Q. And how many children do you have?

A. Two.

Q. Their names, please?

A. Howard Samuel Smith and Barbara Ann Smith.

Q. When was Howard born?

A. Howard was born in '32.

Q. And Barbara?

A. She is 14. That is 1940.

Q. And they are both still living?

(Testimony of Rose Mae Smith.)

A. That's right.

The Court: Up to the time anybody is 50 the question of age is not embarrassing. After 50 it is.

The Witness: You mean even with a woman?

The Court: In court that may be very important. Otherwise your attorney would not have asked you the question.

Q. (By Mr. Lund): Mrs. Smith, I believe you are a partner today with Mr. Smith in the business known as the Boston Shoe Company? [18]

A. That's right.

Q. Going back prior to the time of your marriage to Mr. Smith, did you work for Mr. Smith in the Boston Shoe Company?

A. Yes, I did.

Q. In what capacity did you work, prior to your marriage?

A. Well, I did office work of all kinds, posting, answering the telephone, posting the ledger, making the bills.

Q. Approximately how long prior to your marriage were you working for Mr. Smith?

A. About six months.

Q. And after your marriage did you continue to work in the business? A. Yes, I did.

Q. Doing the same type of work?

A. Yes.

Q. On a regular daily basis?

A. That's right.

Q. And how long did that continue?

A. It has continued up until today.

(Testimony of Rose Mae Smith.)

Q. You will recall, Mrs. Smith, as the documents introduced indicate, that on December 31, 1942, Mr. Smith purchased from you your community property interest in the Boston Shoe Company. Do you recall that? [19]

A. That's right.

Q. Prior to the execution of that agreement and the sale of your community property interest to Mr. Smith, do you recall that you or Mr. Smith had had any disagreements or arguments about the interest that you had in the business?

A. Well, there weren't any arguments or disagreements, but I think that perhaps Mr. Smith would rather I wouldn't be a partner in the business.

Q. You apparently understood that Mr. Smith wanted his interest defined, and your interest defined? A. That is correct.

Q. So that you sold to Mr. Smith your community property interest in the business for approximately $100,000.00?

A. That is correct.

Q. What plans did you have, if any, at that time for the use of that money?

A. Well, at the time we thought that we wanted to set up trusts for the children, so that they would become independent, or, rather, set up something for them independent of us, so that if I wasn't here or my husband wasn't here that they would have a little something of their own.

We thought that if we gave them a gift, or set

(Testimony of Rose Mae Smith.)

aside money for them, or trusts,—we didn't know exactly how to work out the thing—we were getting advice from attorneys on how to set up something, but I know we wanted to set something [20] aside for the children, perhaps buy a piece of property for them, or do something for them, so that they would have something of their own. I didn't know how long I would be here, and I didn't know how long my husband would be here.

Q. You mentioned perhaps buying a piece of property for them. Was there any definite consideration given to that, investing in real estate for the children?

A. Yes, that's right. I wish we would have done it then. We looked at different pieces of property, but every time we looked at something, somebody told us, "This wasn't worth it, and that wasn't worth it," and by the time we turned around property had gone up.

And Mr. Smith or I—I thought to myself I didn't know anything about property, and I don't think my husband does either. The only thing he knows is the shoe business. So as a result we didn't buy any property. As the time passed by, we figured the only thing to do with the trusts—with the money we had given the children was perhaps to invest it in the Boston Shoe Company. That was the only way my husband knew how to make a living, and in investing it that way, and being trustees for them, we could oversee it and see that the trusts —that the business made money for them.

(Testimony of Rose Mae Smith.)

I know of no other outside way of making it. Neither does Mr. Smith know any outside way. At the time we had nothing, we had no property. We bought nothing because we [21] knew nothing about it, although we intended to.

Q. That is the next question. The documents introduced in evidence establish that you did create trusts, respective trusts for the two children in September of 1943. As of that time, did you, aside from these notes which you received from Mr. Smith in payment of your community property interest, did you personally have any property of your own?

A. No.

Q. Outside of this business, the Boston Shoe Company business, did Mr. Smith at that time have any property of any real value?

A. No, neither one of us had anything.

Q. At that time did the children have any close relatives from whom they could expect some substantial inheritance?

A. No. I am sorry, but I have no rich family, or rich relatives.

Q. The only means of providing for their future as of that date was whatever you or Mr. Smith could contribute to them? A. That's correct.

Q. Prior to the creation of these trusts in September of 1943, had either you or Mr. Smith made any gifts to the children?

A. I think that there was a small gift of three or four thousand dollars, I don't recall, whatever the Government [22] allowed. I don't remember

(Testimony of Rose Mae Smith.)

how much it was, but you would have it there in the records, I do think.

Q. Was that a cash gift?

A. I believe so. I am not certain. The records will show that.

The Court: How was that money handled before you created these trusts? What did you do? Did you have a bank account in the children's names?

The Witness: Yes, there was a three or four thousand dollars set up in a savings account for each child.

The Court: And who had the power or the right to draw against it, you or your husband, or both you and your husband?

The Witness: The bankbooks,—neither one of us drew anything against them. The bankbooks, I think, were set up as Howard Smith or Barbara Smith, with us as trustees.

The Court: That is what I wanted to find out. Somebody has to have the power. The children didn't draw against them.

The Witness: Well, I assume——

The Court: At 11 and 3 they could not be entrusted with their own bank accounts.

The Witness: Yes.

The Court: I assume they are trusted now. How old are they now,—the children?

The Witness: My son now is 22.

The Court: Twenty-two. And the daughter? [23]

The Witness: And Barbara is 14.

(Testimony of Rose Mae Smith.)

The Court: Twenty-two and fourteen. So even before you created this trust you deposited this money to their names?

The Witness: We deposited money to their names.

The Court: Subject, of course, to your drawing for their benefit?

The Witness: That is correct.

The Court: All right. How did you handle the interest? You said the books would show. I am just trying to get this, but probably your attorney will bring it out.

The Witness: I don't know anything about the bookkeeping department there. I don't know about the interest on them. All I know is that we would each give them money, and it was set up in a savings account for them. Now, the rest of the bookkeeping——

Mr. Lund: Your Honor. I have the savings book here, if she may just look at it and refresh her recollection as to how it was set up.

The court wants to know the names of the accounts (handing books to the witness.)

The Witness: Here it is. Now I need my glasses. What is the printed part?

Mr. Lund: "Trustee for."

The Witness: "Rose Mae Smith, Trustee for Howard S. [24] Smith," and for Barbara.

Mr. Lund: And it shows how much in the original entry?

(Testimony of Rose Mae Smith.)

The Witness: The original entry was $8,000.00. That was $4,000.00 each for the children.

Mr. Lund: Thank you. And the date? Can you read that date?

The Witness: No, I cannot.

Mr. Lund: December 28, 1942. Is that right?

The Witness: I need my glasses. That is right.

The Court: How long does that precede the establishing of the trusts?

Mr. Lund: The documents show the trusts were set up September 29, 1943, and that is nine months later.

The Court: All right. I just wanted to find out.

The Witness: You see, our purpose, your Honor, was to set something away for the children.

The Court: That is right.

The Witness: You see, not knowing,—as I said before, not knowing what, or how to do it, we knew that we had to set something aside for them.

Mr. Lund: Mrs. Smith, now, wait for the questions.

The Witness: Yes.

The Court: All right, go ahead.

Q. (By Mr. Lund): From the time that you received the notes in September of 1942 from Mr. Smith for your community [25] property interest in the business up until the time that the written trust agreements were executed the following September, did you give serious consideration to investing on behalf of the children in real estate in Los Angeles? A. Yes, we did.

(Testimony of Rose Mae Smith.)

Q. That's all.

A. But it never went through.

Q. When the trusts were created in September of 1943, as you recall,—I think the records show, the documents show that—you gave to Mr. Smith in trust for Barbara one of the $30,000.00 notes of Mr. Smith that you then had; is that correct?

A. That is correct.

Q. And you understood at the time of the creation of that trust that it was on an irrevocable basis? A. That is correct.

Q. You were giving that up for all time, and giving up any control of that money for your own purposes? A. That is correct.

Q. And the money could only be used for the children, according to the terms of the trust?

A. That is correct.

Q. You continued thereafter to provide for the children their education out of other sources of income, and didn't use any of the money in the trust for that purpose? [26] A. Correct.

Q. Now, you recall that at the same time, or the documents I think are dated two days apart, that the trust was created and you entered into a partnership agreement with Mr. Smith and yourself, and with Mr. Smith and yourself also acting as trustees? A. That's right.

Q. And that you purchased from Mr. Smith for $60,000.00 through these notes you had a 30 per cent interest in the partnership?

A. That's correct.

(Testimony of Rose Mae Smith.)

Q. In the business that went into the partnership? A. That's correct.

Q. And that you also purchased from Mr. Smith a 15 per cent in the business for Howard, for whom you were acting as trustee?

A. That's correct.

Q. Do you recall that you received from Mr. Smith for Howard, the beneficiary, with you as trustee, $30,000.00 in government bonds; is that correct? A. That is correct.

Q. And you, in turn, then gave those back to Mr. Smith for the purchase of the interest in the partnership? A. That's correct.

Q. Do you recall any particular reason why it was [27] finally decided to purchase an interest in the business rather than put the money for the children in real estate, or any other investment?

A. Well, as I said before, we looked at different pieces of property, business property, around the city, Los Angeles Street, through there, but not knowing much about it, we asked advice on it, and then by the time we could turn around, the property had gone up 25, 30 per cent, and we felt that not knowing anything about real estate, perhaps it wouldn't be a wise thing to invest in real estate, but to invest the money—at that time the business was a very lucrative one, we were making money then, and we felt that as long as we were trustees for the children, to invest our money in something which we knew how to make money at, and so we figured on the real estate, we didn't know anything about

(Testimony of Rose Mae Smith.)

it, it kept going up in price, and no one would give us any advice on it, so that we felt that perhaps it would be best to invest in the Boston Shoe Company. And that is why that was set up that way, because then my husband could supervise it, to the best of his ability, for the interests of the children.

Q. Do you recall whether you received advice from anyone at that time that you should make the trusts partners in the business, in order to save your own personal income tax liability on the share, the individual share of profits of [28] the business?

A. Well, I don't know anything about the taxes. I know that we were advised how to set up trusts by counsel, by law, but I don't know anything about the income taxes, or anything of that type.

Q. Well, do you recall or can you testify that these trusts were set up, and they became partners in the business, in order to create an estate for the children, or for the purpose of saving taxes?

Mr. Hochman: Your Honor, I object, that the question has been asked and answered, to the best of the witness' knowledge, and at this juncture it is only leading.

The Court: She may be asked that question.

The Witness: No.

The Court: The question may be asked as to her intention. Then when a person answers that it was not to evade taxes or to save taxes the answer is not necessarily binding on the court, because it must be considered against the background of the facts.

(Testimony of Rose Mae Smith.)

All right. Will you read the question, please?

(Question read.)

The Witness: No, they were set up primarily for an estate for the children, because when the children were born, we had always had that in mind. We didn't know exactly how to do it, or what to do, but we always thought of setting [29] something up for the children.

As I said before, my husband and I know nothing about real estate. He only knows the shoe business. We wanted to do something to protect the children. I didn't know how long I would be here, and I didn't know how long my husband would be here, and our purpose was taking care of the children, to see that they would have something.

The Court: All right. Since the son has grown up, has he taken part in the business at all, or what is his occupation?

The Witness: My son right now is continuing his education. He will be home in the next day or two. When he is home in the summer, he usually comes into the office and helps us out, but he is still going to school.

The Court: What school is he going to?

The Witness: Harvard.

Q. (By Mr. Lund): As I understand it, your son completed his undergraduate course at Stanford? A. That is correct.

Q. And is finishing his first year of graduate work at Harvard? A. That is correct.

Q. And when he is home during the summer

(Testimony of Rose Mae Smith.)

months and in the vacation periods, has he worked in the business then?

A. That is correct. [30]

The Court: I haven't had time to look at the trusts, but is there any provision made for any change of trusteeship upon either child attaining maturity, or is there any such provision?

Mr. Lund: The trust provides for the distribution beginning at the age of 25, when the child reaches 25, but there are provisions for anticipation of distribution set up on a formula basis beginning at the age of 21, and there are successor trustees named in the instrument, to whom I will refer and identify by another witness.

The Court: I see. All right.

Mr. Lund: That is all of this witness, your Honor.

The Court: Cross examine.

Cross Examination

Q. (By Mr. Hochman): Mrs. Smith, would it be true to say that the trust arrangements and the partnership arrangements, following so closely, I think a matter of two days, were done with the same thought and basically at the same time? I refer now to September 29, 1943, when the trusts were drawn up by yourself and your husband?

A. Well, this all took a period of time. You see, when the partnership was set up and the trusts were set up, we set money aside for the children, trying to see if we could invest in some other way,

(Testimony of Rose Mae Smith.)

but as long as we couldn't invest it in [31] outside real estate, we decided to invest right into the company.

Q. Now, then, you are the trustee, are you not, of the Howard Samuel Smith trust?

A. That is correct.

Q. And you are the grantor to the Barbara trust?

A. I don't know what you mean by "grantor."

Q. Well, you are the trustee,—to use another word, an administrator, so to speak?

The Court: There is no use of asking her. The documents show that. So let's get down to the matters that this witness can testify to. I presume she signed the documents when they were prepared by the lawyers at the time; isn't that true?

The Witness: That is correct, yes.

The Court: And, of course, the source of the money with which this trust was established was you and your husband?

The Witness: That is correct.

The Court: You put up the money?

The Witness: That's correct.

The Court: And you created the trust?

The Witness: That's correct.

The Court: All right.

Q. (By Mr. Hochman): The money that you gave to your daughter's trust, was it money that you put in, or did you [32] rather put in a promissory note? A. Those were notes.

(Testimony of Rose Mae Smith.)

The Court: Notes that your husband had given you?

The Witness: Given me for sale of my interest.

The Court: For your interest in the community property?

The Witness: For my interest in the community property, that's right.

The Court: All right.

Q. (By Mr. Hochman): You testified that your participation in the business was in the office, is that correct, as you have indicated before?

A. That is correct.

Q. In the period involved here, between 1942 to approximately 1948, when the children were small, were you then in full-time work in the office?

A. Yes, I was. I even did shipping, too.

The Court: Where is the business located?

The Witness: 826 South Los Angeles Street.

The Court: Is it a wholesale business?

The Witness: Wholesale, that is correct.

Q. (By Mr. Hochman): You spoke of purchasing property, perhaps. Where did you plan to get the cash for the purchase? You had a note that was not yet due. You had four notes, I believe, none of which were due.

A. Well, I will tell you something. At that time our [33] business was a very lucrative one. I had planned, and I knew the Union Bank & Trust Company would have given us money any time. My husband's name and reputation was very fine, and if we would have found a piece of property that

(Testimony of Rose Mae Smith.)

we had wanted, I am sure the bank—in fact, we figured that the bank would have given us the money for it.

Q. Do you know a Ben Breiman?

A. Yes, I do.

Q. Who is that gentleman, please?

A. My husband's brother.

Q. Was a loan given to Mr. Breiman in 1947 from the Howard Samuel Smith trust?

A. I don't know.

Mr. Hochman: I have no further questions, your Honor.

Mr. Lund: No redirect.

(Witness excused.)

Mr. Lund: Mr. Hartman.

LeROY E. HARTMAN

called as a witness on behalf of the plaintiffs, having been first duly sworn, was examined and testified as follows:

The Clerk: What is your name, please?

The Witness: LeRoy E. Hartman.

The Clerk: The spelling of your last name?

The Witness: H-a-r-t-m-a-n. The LeRoy is capital "R," sir. [34]

Direct Examination

Q. (By Mr. Lund): Your address, please, Mr. Hartman?

A. 2224 Electric, in Alhambra.

(Testimony of LeRoy E. Hartman.)

Q. Are you employed by the Boston Shoe Company? A. I am.

Q. And in what capacity?

A. Well, as a more or less general manager and accountant.

Q. How long have you been employed in that business?

A. Since July 9, 1938, other than the time I spent in the Armed Service.

Q. You mentioned as an accountant. Are you an accountant by profession or training?

A. No, sir.

Q. But you do bookkeeping?

A. I do bookkeeping.

Q. In that capacity do you have custody of the books and records of the Howard Samuel Smith trust and the Barbara Ann Smith trust?

A. I do.

Q. At our request, did you prepare from those records a summary of the receipts and disbursements and investments of each of those trusts?

A. I did. [35]

Mr. Lund: I might mention, your Honor, counsel has copies of these documents.

Q. (By Mr. Lund): I show you a document headed, "Schedule of Receipts-Disbursements-Investments, Howard Samuel Smith Trust, December 28, 1942, to December 31, 1948," and ask you if you prepared that document accurately from the books and records of the Howard Samuel Smith trust.

(Testimony of LeRoy E. Hartman.)

A. Yes. These reflect exact entries on the books of the Howard Smith trust.

Q. And will you tell us what these various subdivision breakdowns are in this document of three pages? I don't mean the detail of each entry, but it is broken down into two or three parts.

A. The first page shows the receipts into these trust funds, as to where the money came from, and also the disbursements, as to what was paid out of this trust fund.

The second page shows the schedule of investments, and it shows how the money from these trusts were invested, and the third page is a continuation, of course, of the second page.

Q. Now I show you a similar document headed, "Schedule of Receipts-Disbursements Barbara Ann Smith Trust, December 28, 1942, to December 31, 1948," and ask you if you prepared that document.

A. Yes, I did.

Q. And it is an accurate transcription of the books and [36] accounts of the Barbara Ann Smith trust? A. Yes.

Q. And it shows the same information as the one you just testified about from the Howard Samuel Smith trust? A. That is correct.

Mr. Lund: We offer at this time the document pertaining to the Howard Samuel Smith trust as our next exhibit in order.

The Court: It may be received.

The Clerk: Plaintiffs' Exhibit 21 in evidence.

(Testimony of LeRoy E. Hartman.)

(The document referred to was marked Plaintiffs' Exhibit 21 and was received in evidence.)

[See pages 276-7.]

Mr. Lund: And we offer as the next exhibit in order the schedule concerning the Barbara Ann Smith trust.

The Court: All right.

The Clerk: Plaintiffs' Exhibit 22 in evidence.

(The document referred to was marked Plaintiffs' Exhibit 22 and was received in evidence.)

[See pages 278-9.]

Q. (By Mr. Lund): Mr. Hartman, will you explain to us from these documents what the assets of the Howard Samuel Smith trust were as of December 31, 1948?

A. The assets of the trust fund?

Q. Yes.

A. Yes. There was an item, a savings account in the Union Bank & Trust Company—no, that was cleared up. Pardon me. [37]

There were savings bonds, that is, U. S. Series E savings bonds in the total sum of $7,500.00.

Q. In what name were those bonds carried?

A. That is in the name of—let's see. This is Howard—it would be Howard Samuel Smith, or, Rose Mae Smith as trustee for the Howard Samuel Smith trust.

Q. All right. What other assets?

A. Then there were savings accounts in dif-

(Testimony of LeRoy E. Hartman.)

ferent Federal Savings Banks. As an example, Coast Federal, there was $5,060.44; in the Republic Federal Savings there was $5,060.43; in the Western Federal Savings & Loan there was $4,389.76.

Q. In what name were those accounts carried?

A. Those were in the name of Rose Mae Smith, as trustee for the Howard Samuel Smith trust. Then there was the investment in the Boston Shoe Company, which showed at December 31, 1948, $30,181.10.

Q. Thank you. Just briefly in the same manner tell us the assets as shown on the records of the Barbara Ann Smith trust as of December 31, 1948.

A. There were Series E U. S. savings bonds in the amount of $7,500.00, and in savings and loans accounts there were Coast Federal Savings & Loan Association, $4,060.00; the Home Building & Loan Association, $4,060.00; Los Angeles Federal Savings, $4,199.36; Standard Federal Savings & Loan, [38] $4,246.25; and in the investment in the Boston Shoe Company of $35,979.67.

Q. Now, the Series E bonds, and the savings and loan accounts were in what name?

A. They were in the name of Jack Smith, as trustee for the Barbara Ann Smith trust.

Q. Now, do you know if these savings accounts have continued right up to the present date?

A. Yes, they are still there.

Q. And both trusts still have bonds?

A. Still have bonds; the same bonds.

(Testimony of LeRoy E. Hartman.)

Mr. Lund: That is all, your Honor, of this witness.

The Court: All right. Cross examine.

Mr. Hochman: One or two questions, your Honor.

Cross Examination

Q. (By Mr. Hochman): Mr. Hartman, Exhibits 21 and 22 are the complete assets of the trusts, are they not, to your knowledge, as reflected in the books?

A. That's right, to my knowledge.

Q. There are no other properties, real estate or anything else, that is reflected, to your knowledge?

A. No.

Q. Who pays for your services in regard to the keeping of these trusts? [39]

A. It is a part of my job.

Q. With the Boston Shoe Company?

A. With the Boston Shoe Company, that is right.

Mr. Hochman: No further questions.

The Court: All right.

Mr. Lund: I have a short redirect, your Honor, in view of counsel's questions.

The Court: Go ahead.

Redirect Examination

Q. (By Mr. Lund): You testified that those are the complete assets of each trust as of the dates shown. Is that so far as the books and records are concerned?

(Testimony of LeRoy E. Hartman.)

A. So far as the books and records are concerned.

Q. Do you know of any additional assets or claims that the trusts have?

A. Yes, I think there is an error on them. I believe there is a liability—or, I mean an asset in overfiguring of the taxes. The taxes have been figured wrong, and there is a sum of money due the trusts for that overassessment of taxes.

Q. Due from Mr. and Mrs. Smith to the trusts?

A. Due from Mr. and Mrs. Smith, that's right.

Mr. Lund: That is all.

Mr. Hochman: No further questions, your Honor.

The Court: All right.

(Witness excused.)

Mr. Lund: Mr. Smith.

JACK EDWARD SMITH

called as a witness on behalf of the plaintiffs, having been first duly sworn, was examined and testified as follows:

The Clerk: What is your name, please?

The Witness: Jack Edward Smith.

The Clerk: Edward?

The Witness: Yes, E. Smith.

Direct Examination

Q. (By Mr. Lund): Your address, please, Mr. Smith?

A. 2228 North Catalina Street.

Q. And you are a plaintiff in this action, together with Rose Mae Smith? A. Yes, sir.

(Testimony of Jack Edward Smith.)

Q. What is your age, please, Mr. Smith? Your age? A. Fifty-nine, about.

Q. Now, you are in the business of the Boston Shoe Company? A. Yes, sir.

Q. How long have you been? Well, first, tell me what is the nature of that business.

A. Wholesale and distribution of shoes. [41]

Q. And you are located in Los Angeles?

A. 826 South Los Angeles Street.

Q. How long have you been in that business in Los Angeles?

A. In the City of Los Angeles?

Q. Yes. A. Since 1925.

Q. Prior to that time were you in the business?

A. I was in the business in Massachusetts, sir, at Lowell.

Q. Since what date, approximately?

A. Actively for myself since 1919, sir.

Q. Is it a fair statement to say that almost all of your working life has been devoted to this type of business? A. Yes, sir.

Q. You recall, as these documents show, on October 1, 1943, you formed a partnership with your wife and yourself and the two trusts in the business? A. Yes, sir.

Q. For the years immediately preceding that, how was the business conducted,—as a partnership, individual proprietorship, or corporation, or how?

A. Individual ownership.

Q. That is solely and entirely by yourself?

A. That's right. [42]

(Testimony of Jack Edward Smith.)

Q. Prior to December 31, 1942, your wife had some community property interest, however, in the business; is that correct? A. Yes, sir.

Q. Is the shoe business the only business that you have been engaged in in the last years?

A. Practically the greatest part of my life. I am considered a man that knows shoes.

Q. During the 1940's were you engaged in any other type of business? A. No.

Q. Is that true today? A. Yes, sir.

Q. Based upon your experience and knowledge in this business, how essential do you believe the invested capital is to a successful operation of the business?

A. In our type of business capital is very essential, because we anticipate a lot of purchases in advance.

Q. You carry a large inventory?

A. Yes. We buy white shoes for spring in August, and they come in in October and November. We buy fall shoes, like work shoes, in January and February, and we give long datings to customers. We give them a seasonable dating, and they can buy slippers, Christmas slippers, in January, and then they come in in February and March. [43]

Q. Is it true, then, that at all times you need capital?

A. We always need a lot of capital, yes.

Q. What prompted you to purchase your wife's community property interest in the Boston Shoe Company?

(Testimony of Jack Edward Smith.)

A. Is that an essential question, Mr. Lund?

Q. You don't understand it?

A. I mean, is that an essential question?

The Court: Of course, it is essential.

The Witness: Well, there is a lot of family reasons, your Honor.

The Court: But they have to be brought out. It is too bad, but the Government is not suing you. You are suing the Government for some $115,000.00, and you are basing it on the contention that you entered into a partnership with your wife, and you paid her a lot of money, and then that was transferred to your children, and the whole thing has to be gone into to see if it is a real partnership, and what were the facts behind it.

In all these cases—this is just one case—I have told you I handled, so far as I know, a half a dozen of them, and at least three of them were appealed.

The Witness: Well, it is a little private.

The Court: Whenever a person comes into court and sues anyone, all the actions relating to the transaction must be [44] brought out. The answer is, if you did not want that, you did not have to sue the Government. You could just forget about the $115,000.00, but you brought a suit, and you are seeking to recover the money.

Your lawyer would not ask you these questions if they were not material. I am just trying to help your lawyer out.

The Witness: I know you are, your Honor.

(Testimony of Jack Edward Smith.)

Mr. Lund: I might say, Mr. Smith, we are not asking for all the details.

The Witness: There had been quite a lot of disagreement between Rose and I prior to that, particularly about the amount of charity that I used to give away. She thought it was too much, to the point that I wasn't home for Christmas and New Year's in '42. Does that tell you enough, or would you want to know more?

Q. (By Mr. Lund): At least, the two of you were not in agreement?

A. We were not in agreement for quite a while. She felt that she was working, and she has got—she didn't agree with the Government. She thought she had a half, and I was doing too much of it, giving it away, I was giving it around. So Gittelson and I figured out a way that we can pay her out, and give her a big interest. We paid her 10 per cent interest, I believe, on our notes, instead of the normal interest. [45]

The Court: Well, you owned the business, however, before you were married?

The Witness: On community property, your Honor.

The Court: I know, but you owned the business before you married her?

The Witness: Yes, I did, but after she came into the business, that had nothing to do with the case, she was supposed to be a partner.

The Court: Oh, that isn't the point. We will

(Testimony of Jack Edward Smith.)

decide that. You owned the business before you married,——

The Witness: That's right.

The Court: ——the present Mrs. Smith?

The Witness: That's right.

Q. (By Mr. Lund): As of the time you married Mrs. Smith, you owned the entire business as your sole and separate property?

A. That's right.

Q. However, for the next 11 years after you were married, you contributed services to the business which created in Mrs. Smith a community property interest to the extent of half the value of your services; is that correct?

A. That's right. But you must remember she worked too, sir.

Q. Well, then, that worked both ways?

A. Yes.

Q. The net result of which, as of December 31, 1942, [46] was that both you and she felt it desirable to separate her interest and your interest; is that correct?

A. I felt that way, sir, yes.

Q. Then it was your personal desire to spell out her interest and pay off for her community property interest, so that the business from then on would be your sole and separate property; is that right? A. That's right.

The Court: What did you value the business at the time you gave her $100,000.00 in notes? Was that the amount?

(Testimony of Jack Edward Smith.)

Mr. Lund: Just a few thousand over. $102,-000.00.

The Court: What did you figure the value of the business to be?

The Witness: If I remember right, your Honor, —I am a businessman, and I took advice of good lawyers, and the accountants, and we figured what the business was, what actually was there, and other considerations. It is such a long time, 11 years,——

Mr. Lund: You haven't answered the judge's question. Do you recall what you valued the business at at the time?

The Court: What did you value the business at at the time you bought her out for $102,000.00?

The Witness: We valued everything she had there, with the exception of my separate property.

Mr. Lund: You still haven't answered the question.

The Court: The business was yours, except such as you [47] contributed to it through your earnings,——

The Witness: Yes, sir.

The Court: ——through running it, and that became community property?

The Witness: That's right.

The Court: All right. Now, you said she felt, because she worked in the business for a number of years, that she had a community interest?

The Witness: Yes.

(Testimony of Jack Edward Smith.)

The Court: And you bought her out at $102,000.00?

The Witness: Yes.

The Court: Now, the question I am asking is: What did you figure the value of the entire business to be, from which you carved out this $102,000.00 interest?

The Witness: I would have to look at the records, sir. I don't remember. I can't remember. We figured it at more than $102,000.00. We paid her double, and I think we valued it at a little more than that amount. I don't remember.

The Court: You didn't give her the entire value of the business, did you?

The Witness: No.

The Court: Just her interest?

The Witness: I gave her her interest only.

The Court: And what about your interest? What did you value your interest to be? The same as hers? [48]

The Witness: No, a little more, your Honor, because I had a certain amount of separate property before I married her.

The Court: Now, what was that amount, do you know?

The Witness: I don't remember, your Honor.

The Court: I see. All right.

Mr. Lund: Your Honor, we have a statement as of June 30, 1942, which I presume would be pretty close to the figures. I will show it to counsel, and maybe we can introduce it.

(Testimony of Jack Edward Smith.)

The Court: All right. Evidently he doesn't remember.

The Witness: I don't remember the exact amounts, sir.

The Court: All right.

Mr. Lund: Your Honor, I think counsel would stipulate that the records of the company show that as of December 31, 1942, the total capital recorded was $254,277.68. Do you so stipulate?

Mr. Hochman: So stipulated, your Honor.

The Court: All right.

Q. (By Mr. Lund): For her community property interest in the business, at that time you gave Mrs. Smith some notes? A. Yes, sir.

Q. Do you know whether or not those notes could have been cashed at any bank?

A. Yes, she could have gone to the Union Bank and cashed them very easily.

Q. The Union Bank, you say? [49]

A. Yes, sir.

Q. Were you at that time doing business with the Union Bank? A. Yes, sir.

Q. Have you all the years?

A. I think since 1930. Since 1930.

Q. As of that time, or thereabouts, had you had any plans to make any gifts to your children?

A. Yes, sir.

Q. When did you first have such plans, approximately?

A. Well, we had the plans for a long time. On or about 1941 we felt that we were financially a

(Testimony of Jack Edward Smith.)

little bit stronger, you know, and we could spare larger gifts to our children, and we started about that time to negotiate with our counsel, to plan a will, an entirely family setup, or trusts, where, as a part of my will, sir,—if I may say now, it was entire family plan to provide for the children. We got Barbara in 1940, and became concerned, because I am about 45 years older than Barbara, and——

Q. Well, in any event, in 1942, I believe the passbook indicated you gave a gift of $4,000.00 to the children? A. That's right.

Q. And as of that time you had been and were discussing with your counsel a means for creating gifts for the children? [50]

A. That's right, sir.

Q. As of that time, the first of 1943, what thoughts, if any, did you have, or discussion with your counsel, relative to how you would invest the gifts for your children?

A. Well, at that time we were real estate-minded. When we planned originally, Rose was going to go into the real estate business, and the money that we would give the children we would invest in real estate, also, sir.

Q. Was there any particular reason that you can recall why you abandoned the idea of investing in real estate?

A. Well, at that time it required—the business required a lot of my time. I used to go back east very often, between seven and eight times a year,

(Testimony of Jack Edward Smith.)

by train, not always being about to get back on time on account of accommodations, you know. You remember those days.

Q. Traveling was pretty bad?

A. Yes, and I was out. Our salesmen left us, and I covered territory, and time went too fast, and I didn't have a lot of time to investigate the propositions they brought to us.

Q. Did you have specific propositions brought to you to invest in real estate on behalf of the children?

A. Yes, sir. It was so well known, even before the trusts were formed, and everybody in the city already knew that we had the trusts, and real estate men, and insurance men, [51] everybody approached us, to the point where we had to get men out of the place so they wouldn't disturb us.

Q. Did you actually look at physical sites of property for investment?

A. Yes, we did. We did. We looked at a lot of them.

Q. Do you know of any relatives that either of the children have, other than you and Mrs. Smith, from whom they could expect an inheritance?

A. None, sir.

The Court: You didn't expect them, on growing up, to go into the business?

The Witness: Yes, I did. I expected my son to be in it.

The Court: But he isn't?

The Witness: Well, he is still young, sir. He is

(Testimony of Jack Edward Smith.)

only 22. He hasn't finished his education, and he is a good kid, so we don't want to disturb him.

Mr. Lund: You still have some hopes or expectations that he will get into the business?

The Witness: I hope.

The Court: What is he doing at Harvard? What is he specializing in? What is his major? What was his major at Stanford? Tell me what his major was, and I can draw the inference. What was his major at Stanford?

The Witness: He started with law, and he shifted to chemistry, and now he is going back to law. [52]

The Court: Now he has gone back to law?

The Witness: Yes, sir.

The Court: He is going to Harvard Law School now?

The Witness: He is accepted into Harvard Law School now.

The Court: All right. And you think he is going to go into the shoe business?

The Witness: I think he will. Like all lawyers, I think he will eventually end up——

The Court: Then I think you are sending him to the wrong school. A man with a Harvard law degree is not going into the shoe business. He will be too proud of his Harvard degree to go into the shoe business. He may be different.

Mr. Lund: I was kind of amused, your Honor, because I am a Harvard Law School graduate, and

(Testimony of Jack Edward Smith.)

I am amazed at the number of my law school classmates who have gone into business.

The Court: Perhaps he is different. Let's go on.

Q. (By Mr. Lund): As of the first of 1943, and just prior to the time in 1943 that these trusts were created, you had, I believe, some bonds. Do you recall that in creating the trusts, you gave $30,000.00 in bonds to Mrs. Smith in trust?

A. Yes, I gave Mrs. Smith $30,000.00.

Q. And you had some other bonds, you recall, at that time?

A. Yes, we had additional bonds besides those we gave out. [53]

Q. Do you recall, roughly, how much you had in bonds?

A. I don't. I would have to look at the records.

The Court: I forget, but was it $30,000.00 for each?

Mr. Lund: $30,000.00 for each.

The Witness: Yes, we had a lot more than that. We had a lot more bonds than that.

Q. (By Mr. Lund): You gave in trust for Howard $30,000.00 of those bonds; is that correct?

A. Yes.

Q. And Mrs. Smith gave in trust to you for Barbara—— A. The note.

Q. ——the $30,000.00 note; is that correct, sir?

A. That's right.

The Court: After the surrender of those, you still say Mrs. Smith continued as your partner?

(Testimony of Jack Edward Smith.)

The Witness: After the surrender of what, your Honor?

The Court: Of the bonds, and the cancellation of the notes? Mrs. Smith continued as a partner in the business after the children came in as partners?

The Witness: She came back as a partner. There was quite a little unhappiness because she was no partner, so she came back again.

The Court: So she came back again?

The Witness: I had to take her back again.

The Court: That is right. So that you bought her out? [54]

The Witness: I had to take her back again.

The Court: And when you took her back again, she was an equal partner, except as to such portion as the children received?

The Witness: No, she was not an equal partner; only a partner for 30 per cent.

The Court: And what part was your share?

The Witness: I was 40 per cent, my wife was 30, and the children were 15 per cent each.

The Court: All right. I think this is a good place to stop. I wanted to reach a good stopping point. We will adjourn until 2:00 o'clock.

Mr. Lund: Fine.

(Whereupon, at 12:10 o'clock p.m., a recess was taken until 2:00 o'clock p.m. of the same day.) [55]

The Court: All right, gentlemen, cause on trial.

JACK EDWARD SMITH

called as a witness on behalf of the plaintiffs, having been previously duly sworn, resumed the stand and testified further as follows:

Direct Examination—(Continued)

Q. (By Mr. Lund): Mr. Smith, in September of 1943, when you gave three $10,000.00 bonds to Mrs. Smith in trust for your son Howard, did you have any other assets of substance outside of your business?

A. We had some bonds; a few bonds.

Q. Do you have a recollection, roughly, what they amounted to? A. No, I don't.

Q. Well, are we talking about $100,000.00, $5,000.00, or $25,000.00, or what?

A. No, they didn't go into the hundreds of thousands. We had a few bonds.

Q. Do you recall that in December of 1942 you gave a $4,000.00 gift to each one of your children?

A. Yes, I do.

Q. That was cash, was it? [56]

A. Yes, I believe it was cash, yes. It was checks.

Q. How long, if you recall, prior to September of 1943, when this trust was created, had you been planning and discussing and trying to arrange some gifts for your children?

The Court: I think he talked about the real estate venture. Didn't you go into that this morning?

The Witness: He is asking how long before.

Mr. Lund: I didn't think I had covered it with

(Testimony of Jack Edward Smith.)

this witness, your Honor. Mrs. Smith did testify in some detail, your Honor.

The Court: Oh, I thought he said, too, that it was even before they started the trusts he went to real estate men.

Mr. Lund: You are right, your Honor. I believe the witness testified that he went out and looked at some properties.

The Court: I merely want to avoid repetition.

Q. (By Mr. Lund): You did testify that you looked at some real estate property, didn't you?

A. Yes, but it was quite a long while before '42. I mean it was quite a long while.

Q. Between the time of the December 1942 purchase by you of your wife's community property interest in your business, and the time of the creation of the trusts on September 29, 1943, were you still thinking of the possibility of investing some of the money in real estate for your children?

A. Yes, we did, but it was—— [57]

Q. What was the purpose of creating this trust for your son?

A. To create something for the next generation, for my son, so that if anything happens to him like happened to me, that he wouldn't be destitute.

Q. Who is Mr. Gittelson that you referred to?

A. Mr. Gittelson is our family and business counsellor.

Q. How long has he been? Is he an attorney?

A. At least since 1938.

Q. He is an attorney in Los Angeles?

(Testimony of Jack Edward Smith.)

A. Yes, he is an attorney.

Q. Is he, so far as you know, a tax specialist?

A. No; no.

Q. Then you consulted him in connection with these transactions, and the purchase?

A. We consulted him for a will, and the setting up of the trusts.

Q. And the partnership?

A. The partnership that has—you mean the new partnership, with the children, you are talking about?

Q. Yes, in September and October, 1943.

A. Yes, we consulted on everything, that's right.

Q. Is it your testimony that about the time you entered into the trust agreements you executed a will?

A. Yes, it was a part of a family arrangement.

Q. Now, I believe the instruments show that you gave to Mrs. Smith in trust for your son Howard three $10,000.00 bonds. A. Thirty?

Q. Three $10,000.00 bonds; is that correct?

A. That's right.

Q. And you understood that that gift was on an irrevocable basis, that you could not touch it for your own purposes?

A. That's right. We understood that it was irrevocable.

Q. Was there any effort to keep secret the fact that you had entered into this trust agreement?

A. No. We consulted with Mr. Cameron of the Union Bank practically for years, sir, to set up our

(Testimony of Jack Edward Smith.)

family affairs, and he may have recommended something like that before we even went to Gittelson, from the trust department.

Q. Did you at any time mention to either one of your children that you and your wife had established a trust for them?

A. We did. We told them practically everything.

Q. Your daughter in 1943 was only about three years old, as I recall?

A. Well, when she heard Howard ask something, she usually asked something too, if she has got something too.

Q. Have you ever had occasion to discuss with your son Howard his trust, so to speak? [59]

A. Yes, sir, we often did.

Mr. Hochman: We object, your Honor, as to the comments of the son. That would be hearsay.

The Court: Overruled.

The Witness: Shall I say?

The Court: Go ahead.

The Witness: Yes, I have talked to Howard many times. I think when he was about 17, when he entered college, he asked me when he could be able to use his own money, and I told him to read the trust. I don't know whether he did or not, but I told him that we had a copy at home and he could read it. I believe he did.

Q. (By Mr. Lund): As of the time this trust was created in September of 1943, did you or Mrs. Smith have any close relatives in Los Angeles?

(Testimony of Jack Edward Smith.)

A. Yes, I have a brother and a brother-in-law, and Mrs. Smith has a brother.

Q. Had any of those as of that time been successful in business? A. No.

Q. Did you have any relatives that either of you had confidence in?

The Court: I believe you asked him that this morning. You asked about whether he had any relatives from whom they might inherit. You asked him that this morning. [60]

The Witness: No.

Mr. Lund: I am developing now as to the relatives on the question of their possibility as trustees.

The Court: Oh, go ahead.

Q. (By Mr. Lund): Were there any relatives in Los Angeles in whom you had confidence to handle the funds of the trusts?

A. No. I had to assist most of them.

Q. You had to assist them financially?

A. Yes, most of them. They had a hard time.

Q. Who is Ben Smith?

A. Ben Smith is my brother.

Q. And I believe he was named in the trust instrument as an alternate?

A. As an alternate, yes.

Q. And who is Mr. Ben Finkle?

A. Ben Finkle is a perfect stranger. He was an accountant at the time for the Boston Shoe. He is associated with Mike Pritkin, and he is one of the accountants, or junior partners. Not having anybody else, we put him in.

(Testimony of Jack Edward Smith.)

Q. He was no relative of yours?

A. No relative at all.

Q. He was just a personal friend?

A. Just a paid employee.

Q. Can you tell us why it was ultimately decided by [61] you and your wife to put the gifts which you were going to make your children in trust in an investment in the business, by way of creating the partnership?

A. There is a little tie-in to this. I had to take my wife back as a partner. She was very unhappy when she was out, and when we started discussing that, why, it sounded all right to take in and to form, to get the whole family into it, and that was part of the plan. That is how we came to form the family partnership.

Q. Did you discuss or seek advice from Mr. Gittelson, or Mr. Cameron of the Union Bank as to how——

A. I have talked to Mr. Cameron——

Q. Wait until I finish the question—as to how you should invest any gifts which you made to your children?

A. Yes, we did. We were even going to buy Union Bank stock with it. If you want to go in and explore the whole thing, it is years of thinking. We had a lot of investments in mind.

Q. Did any of those advise you against putting the trust into the partnership?

A. No, sir, they all recommended it. I talked to the president or the vice president of the Union

(Testimony of Jack Edward Smith.)

Bank. I don't remember now whether he was president or vice president, but he was a close friend of mine.

I talked to Mr. Lippman about it, and Mr. Lippman knew [62] months before,—I mean months, it would be many months before, of our plans and he recommended it.

The Court: But you used your own judgment at all times as to what to do with the money in the fund?

The Witness: Yes, I finally made my own mind up. I thought it was all right.

The Court: I notice there are some stocks of building and loan companies which are in the portfolios, as it were, of each of the trusts. Now, you used your own judgment in taking the funds and investing them in that way in that kind of security; isn't that true?

The Witness: Not all my own. Mr. Hartman discussed a lot of that. Mr. Hartman picks them out, and he asks me, and I say it is all right. Sometimes he picks a company that I——

The Court: Did I understand—you didn't say, but I think your counsel said this morning that you have not used any of the interest on the securities in the portfolios. You know what I mean by the portfolios?

The Witness: Yes, I know.

The Court: The bankers use the expression.

The Witness: I know that. I understand you.

(Testimony of Jack Edward Smith.)

The Court: You are carrying an account, in other words, that has so many things in it?

The Witness: We are trying to create a portfolio right now. I understand you, sir. [63]

The Court: All right. Now, as the moneys came in, you used your own judgment as to whether to leave them in the bank, or how much to leave, and what to invest elsewhere?

The Witness: I accepted the responsibility, but it was usually done by Mr. Hartman.

The Court: Now, your son, since he has become of age, has not been consulted as to what has been done with your money, is that correct?

The Witness: No, he has not been consulted.

The Court: And you, being the good father that you are, have paid for his education?

The Witness: Yes, sir.

The Court: Out of your own funds?

The Witness: That's right.

The Court: And you have not drawn on these funds?

The Witness: No, sir.

The Court: And you do not intend to charge his estate with the cost of his education?

The Witness: No, sir.

The Court: But he has no power to draw against it?

The Witness: No, sir.

The Court: And your daughter has not, because she is not of age?

The Witness: No.

(Testimony of Jack Edward Smith.)

The Court: But he, even though he is of age, cannot [64] draw on it?

The Witness: He can't until he is 25.

The Court: I believe you said that when he became 25 years of age there is some provision as to how he can draw it all out?

The Witness: No, part of it. It was Mr. Cameron's idea at 25, 30, 35, 40, and if he doesn't know what to do with it after 40, why, he is not responsible for it.

The Court: I see. You finally decided to terminate the trust when he is 40?

The Witness: Forty. If he doesn't know what to do with it at 40—why, I mean I didn't decide. That was the advice we received.

The Court: All right.

Mr. Lund: Along the lines of your Honor's inquiry, within the last year or so——

The Court: As I say, gentlemen, I am at a disadvantage. I haven't had the time to look at the exhibits. It may be that it is in the trust, but, as you know, these were only introduced today, and I have been too busy with other matters to be able to read them. I will read them in due time, but, as I say, I am propounding these questions on the basis of what you have told me is there. I haven't read them myself.

Q. (By Mr. Lund): Within the last year or so, have you and/or your wife made gifts of cash to your son Howard? [65]

(Testimony of Jack Edward Smith.)

Mr. Hochman: I object, your Honor, as to what is being currently done as not important.

The Court: No, the entire relationship may be gone into. Go ahead. You may answer.

The Witness: When Howard graduated from Stanford, we each gave him a $3,000.00 gift, and I believe it was so reported.

Q. (By Mr. Lund): That was about a year ago?

A. A year ago, when he graduated from Stanford.

Q. Now, at the time you mentioned Mr. Cameron and Mr. Gittelson, you were talking to them——

A. And Mr. Lewis from the Union Bank.

Q. ——you were talking to them about your future plans for your children, and so on, and did any of those gentlemen you were consulting advise you you should create a trust and make the trust partners in your business in order to avoid or save income taxes?

A. No, the income taxes was not an issue concerned.

Q. Well, was that done, was the trust created and the trust made a partner in the business for the purpose of saving you individual income taxes?

A. That was not the consideration, sir. It may have been explained that it might save, but that was not our consideration for creating the trust.

The Court: But 1942 was the beginning of the high surtax, [66] the wartime period, wasn't it? You knew that, didn't you?

(Testimony of Jack Edward Smith.)

The Witness: I believe at that time taxes became high.

The Court: It began in 1940, or I believe the first one was in 1941, and in 1942 they began to impose them. You see, in 1942 we were already in the war, and in 1940 they began thinking about it, so the high tax periods began around that time; isn't that true? Isn't that your recollection?

The Witness: Your Honor, when I talked to Billy Lewis of the Union Bank, who was a good friend of mine, and I talked to these people before I came to Gittelson, I went to them for first advice, and the proposition of taxes was not considered by either one of us with these two gentlemen.

The Court: All right.

Q. (By Mr. Lund): What was the purpose, then, of making the trusts partners in the Boston Shoe Company's business?

A. Well, the money began to be needed. My statement didn't balance very good, if I remember right. I am giving you the best of my recollection. I needed money back in my business. I think my liabilities were a little bit out of balance, I showed too many liabilities against assets, and we needed a little bit more capital in the business, too, and it would have helped. And at that time I had an idea that we will be the outstanding distributors on the West Coast, we [67] will cover all the 11 states, and the more money we will have, the more business we can do.

(Testimony of Jack Edward Smith.)

The Court: How were you getting money for the creation of this trust?

The Witness: Well, first we were going to give it to the kids, and then we thought we could invest it well in our own business.

The Court: Taking back your own money; is that it? You didn't bring in any outside money?

The Witness: Well, we gave it away to them, and we brought it back again.

The Court: I see. It was that way.

The Witness: That's the way we were advised to do it.

The Court: And you paid your wife $100,000.00, and then took her back as a partner?

The Witness: Took her back as a partner.

The Court: All right.

Q. (By Mr. Lund): At that time the business was reasonably prosperous?

A. Yes, we were making money at that time.

Q. And you were expecting it to continue to be reasonably profitable?

A. That's right. I took in another partner. I took in Herman.

Q. We will come to that in a moment. From time to time [68] during the period from 1943 to 1948 did the business borrow short-term loans from the bank?

A. Yes, I think we went in quite often for money.

Q. In connection with those borrowings, did the

(Testimony of Jack Edward Smith.)
bank receive copies of the trust instruments and the partnership instruments?

A. Yes, sir. The bank was always—I think the bank received a copy as soon as the trust was formed, sir, I believe.

Q. Of both the trust instruments and the partnership instruments?

A. Yes, sir, I think they had the whole thing. As I remember, when we went to them, we made out a separate account for Jack Smith, a separate account for Rose Smith, a separate account for Jack Smith, trustee for Barbara, a separate account for Rose Smith, trustee for Howard, and all that was discussed with bank officials.

Q. Beginning from the time of October 1, 1943, when the partnership was formed, were your insurance contacts and other instruments written in the names of the four partners, yourself, Mrs. Smith, and your son and daughter?

A. Everything was changed. The name was registered in the county. The trade name, Boston Shoe Company, was registered under all the four names.

Q. And the insurance and all the other contracts? [69]

A. Everything was properly changed. We did everything that we were advised.

Q. How about your trade customers, and so on? Did they have any knowledge of the change in your nature of doing business as a partnership?

A. Some of them did, and it was spoken about, but most of our suppliers knew about it.

(Testimony of Jack Edward Smith.)

Q. Now, who is Mr. Herman Weishaupt?

A. Mr. Herman Weishaupt was an employee of the Boston Shoe Company.

Q. For how many years prior to 1945?

A. He started on or about 1933.

Q. And going into 1945, what was his capacity? Just prior to the year 1945, what was Mr. Weishaupt's capacity?

A. He was some sort of an assistant to me in buying and supervising.

Q. And he came in as a partner as of January 1, 1945; is that correct? A. That's right.

Q. With a 10 per cent interest?

A. A 10 per cent interest.

Q. And that partnership continued up until June 31, 1948? A. That's right.

Q. Now, subsequent, and from the period of June 31, [70] 1948, on to the present time, you have continued the partnership, with you, and your wife, and yourself and your wife as trustees?

A. Yes, sir.

Q. And the respective interests of each of those four partners is what since 1948?

A. It is separate and distinct. Each one gets his own.

Q. What are the partnership interests?

A. It is 40, 30, 15 and 15.

Q. You have 40, Mrs. Smith 30, and each of the trusts 15; is that correct? A. That's right.

Q. And that is true from July 1, 1948, up to the present time? A. That's right.

(Testimony of Jack Edward Smith.)

Mr. Lund: That is all.

The Court: Just before the cross examination begins, I want to ask one question as soon as I get some of the dates on some of these exhibits. Just a moment.

Is this declaration of trust, which is Exhibit 7, dated September 29th, is that the final form, or is that the——

Mr. Lund: That is the final form, the only form.

The Court: The only form?

Mr. Lund: That's right.

The Court: That is dated the 29th of September, 1943. [71]

The Witness: Yes, sir.

The Court: And these schedules which your accountant or bookkeeper introduced as Exhibits 21 and 22 show that the gift of bonds from your wife to each of the children was dated September 28th. That is the day before.

The Witness: I guess the lawyer did it that way.

The Court: Well, I mean, the gift was made the day before the trust?

The Witness: The gift was set away a long time.

The Court: Was set away?

The Witness: For practical reasons the gift was set away a long time. I mean, the legal papers do not show.

The Court: Now, where is that amount—I can't tell, and I am not a bookkeeper—when was that money that you gave to the children turned back to yourself into the business? You said you gave it

(Testimony of Jack Edward Smith.)

to them as a gift, and then took it back in exchange for giving them an interest in the business.

The Witness: As the contracts were completed.

The Court: When was that taken out of these separate accounts and turned over to you, to the Boston Shoe Company, in payment for the interests you gave by this deed of trust?

The Witness: Practically at the time. We were in the lawyer's office, and the things were made. These things were started a long time before.

The Court: All right. Show me on the books of your [72] company when this $60,000.00 was taken out of the accounts of the children and put back in the Boston Shoe Company, so that you could draw against it, not as trustee, but as the managing partner. Show me that.

The Witness: I guess our books will reflect that. I am not an accountant.

The Court: Well, it does not reflect it there. That statement does not show that it was ever taken out, that $30,000.00, if I read it correctly. Let the bookkeeper show me where it shows that this money was taken out and paid into the partnership for the 15 per cent interest. I would like to see it either here or on the books of the company.

The Witness: It is there, your Honor.

The Court: Just a minute.

Mr. Hartman: Do you want me to answer that, your Honor?

The Court: Yes.

(Testimony of Jack Edward Smith.)

Mr. Hartman: On that schedule under "Notes Receivable,"——

Mr. Lund: Page 2.

Mr. Hartman: ——on page 2 of the Barbara Ann Smith Trust is shown "9/28/43, Gift from J & R Smith, $30,000.00."

The next entry is "10/1/43, To Boston Shoe Co.," and a credit or withdrawal from the investments of the trust is this $30,000.00, and the balance, which is your last column, as of 12/31/48, there is no balance from that.

The Court: Will you show it to me here? Show it to me, [73] please. I don't know the bookkeeping setup.

Mr. Lund: He is referring here to notes receivable, September 28, 1943. This is the gift of the $30,000.00 note, and then the partnership was formed on October 1, 1943, and it says, "To Boston Shoe Co., $30,000.00."

The Court: In other words, you washed the note out against the hypothetical $30,000.00?

Mr. Lund: The note was used to purchase the 15 per cent interest in the partnership, yes, in the Boston Shoe Company.

The Court: I see. So that this $30,000.00——

Mr. Hartman: You see, your Honor, this first page is the schedule showing the receipts and disbursements into and out of that trust fund.

The Court: Yes, I know, and it shows the receipt of $32,250.00.

Mr. Hartman: $32,250.00 into that trust fund.

(Testimony of Jack Edward Smith.)

The Court: That is right.

Mr. Hartman: You see, and it does not show there whether it was in the form of a note, or bond, or whatever it was, and it is just like any item shown there.

The Court: I see.

Mr. Hartman: And this is just a schedule of the investments. As an example, let me show you and point out——

The Court: I am trying to see, as to this $30,000.00, in what form it got into the company. As it is here, it was [74] merely by cancellation.

Mr. Hartman: There is a note receivable received by the trust on 9-28-43 in the amount of $30,000.00. Then it was given to the Boston Shoe Company on October 1, 1943, the $30,000.00, so that cancelled out that investment, that item of investment.

The Court: I see. All right. Go ahead now, Mr. Hochman.

Cross Examination

Q. (By Mr. Hochman): Mr. Smith, would it be a fair statement, sir, to say that you are the Boston Shoe Company?

A. I don't quite understand you, sir.

Q. Well, let me go back: Would it be a fair statement to say that due to your experience in the line of business in which you are operating, to your know-how, to your contacts, your industry and your skill, that you would be what we would term the guiding hand of the Boston Shoe Company?

(Testimony of Jack Edward Smith.)

A. Yes, I am there all right, if that is what you want to bring out. I imagine they could operate without me.

Q. I just want to know what is there. In other words, you are——

A. I am the head man—I am one of the head men of the Boston Shoe Company. It is running with Mr. Hartman and running with other people without me. I was sick this year, [75] and it was pretty good without me, too.

Q. Do you make major policy decisions, sir?

A. When the others fail—when all the employees fail, they come to me. Maybe about one per cent. I beef about a lot of them later.

Q. Do you maintain general supervisory control of the Boston Shoe Company?

A. What I supervise actually is the buying, the original purchase. After that it is done by employees, sir.

The Court: You have never consulted the children in regard to the matter, or your son since he has become mature, in regard to the conduct of the business, have you?

The Witness: Well, he comes into the business, your Honor, and we talk things over.

The Court: I know he works when he is not studying. Evidently he is a very studious young man.

The Witness: Yes, I have talked to him. I have talked to him about policy. Ever since he was 13

(Testimony of Jack Edward Smith.)

or 14 years old he has made recommendations. He is quite a brilliant kid.

The Court: I have no doubt about it. I have no doubt about it.

Q. (By Mr. Hochman): Mr. Smith, you mentioned that on December 31, 1942, through four notes executed by you at that time in favor of your wife, you bought her interest in the business. You also testified, sir, that those notes were at [76] 10 per cent, and you were being fair in terms of your wife. Well, sir, was it your intent at that time to execute 10 per cent notes with the thought in mind that she would turn around to the bank and sell them at 10 per cent?

A. My thought at that time was to take Mrs. Smith out of the business, to take her share out of the business, and the rest of it was all consultations. She had some advice too in that time.

Q. We have had certain discussions, sir——

A. I don't get you.

Q. We have had certain discussions in your testimony and that of your wife relative to the purchase of real estate. A. Yes, sir.

Q. When I questioned Mrs. Smith, she mentioned the fact that your credit—and I don't doubt this—was good, and she could take the notes to the bank and get the money.

A. That's right.

Q. But what your initial testimony was that the 10 per cent granted on the notes, which was a considerable amount of money, was because it was your

(Testimony of Jack Edward Smith.)

wife's. Now, then, sir, I question you as to whether when you executed those notes was it your contemplation on December 31, 1942, that in the near future, for the purpose of getting cash to buy realty, your wife was going to sell the notes?

A. Not sell them; borrow on them. She could borrow on [77] that. She could put them up as collateral.

Q. Could she have borrowed on a six per cent note?

A. She could have borrowed perhaps on five.

Q. Do you know, sir, a Ben Breiman?

The Court: Wherein would that be material? As a matter of fact, if the bank lent her money on your note, the bank was merely banking on your credit, and the bank probably would have lent her money if you had endorsed the note with her, regardless of these notes to her, wouldn't they?

The Witness: Yes, but here she had something separate. She had something that was positively her own, your Honor.

The Court: But it wasn't secured by anything. You could sell your business the next day, and go broke, and she could not have any recourse on the community property, because she had transferred it to you, if it was a valid transfer. Under the law, you could not dispose of the business, and nobody would buy your business without your wife's signature, but with this contract, you could go out on the open market and sell the Boston Shoe Company, and she would not even have to be consulted.

(Testimony of Jack Edward Smith.)

The Witness: Yes, but I couldn't sell it before her getting paid, under the laws of California, with filing escrows, et cetera.

Q. (By Mr. Hochman): But those notes, Mr. Smith, were not payable, were they, for a year, or two, or three? In [78] other words, if you turned around on January 1, 1943, and sold the Boston Shoe Company, you would not owe your wife on the first $30,000.00 note anything until December 31st of 1943?

A. Well, there was no such intentions. I mean, you are working up——

Q. We are not trying to.

The Court: Just a minute. That is all right. He has answered. What he is referring to——

The Witness: The bank could have lent us $150,000.00 on six months, and we could have sold the business the next day, and the bank would have to wait six months before they would get the money. But, I mean, that isn't the way credit—we don't grant credit on that basis.

The Court: You see, what he is referring to here: On this contract the notes were——

The Witness: I needed money at that time.

The Court: What is the expression?

Mr. Hochman: Times notes, your Honor.

The Court: ——time notes.

The Witness: The time was why she got such a large interest.

The Court: I see. They were time notes, and

(Testimony of Jack Edward Smith.)

none became due earlier than one year, and the others every year thereafter. [79]

The Witness: Your Honor, if they weren't time notes, I could maybe have gotten the money at the Union Bank for four per cent, and that was the consideration.

The Court: I see. All right.

Q. (By Mr. Hochman): Mr. Smith, do you know Ben Breiman?

A. Ben Breiman is my brother, full-fledged brother, from the same father and the same mother.

Q. Now, you are trustee, are you not, of the Barbara Ann Smith trust? A. That's right.

Q. Do you recall a loan made, sir, on 11-6-47 to Mr. Breiman for $2,500.00 from the Barbara Ann Smith trust? A. I perhaps recall that,——

Q. Now, then, sir,——

A. ——with interest.

Q. No.

A. Yes, sir, with interest, and there was good intentions in that, too. It was perhaps to buy a piece of property for the Barbara Ann and Howard Smith trusts. It was to buy a piece of property, and we let him do the negotiations. It was to buy the piece of property that Rose and I own now. It was property bought, and we were going to buy it for the kids, and we didn't think it was a good investment.

Q. In other words, you gave him $2,500.00? [80]

A. $5,000.00, I believe.

Q. Yes, $2,500.00 from each trust?

(Testimony of Jack Edward Smith.)

A. That's right.

Q. And he was to purchase a piece of real estate? A. Yes, sir.

Q. Then why did he pay interest on the money, sir? A. Well,——

Q. Was he your agent for the purpose of purchasing real estate?

A. Well, I was busy, and I wanted Ben to act as the buyer. We had certain intentions, see, and then after he made the sale, to turn the property over perhaps to the trust. That was the intention, but it turned out that I took it over rather than the trust. And there was a reason for that, too, so I took it over.

Q. And then $20.28 was paid on that as interest?

A. That's right. The reason I took it over, you see, was a legitimate reason.

Q. Nothing——

A. It was a perfectly good reason.

Q. The Government does not intend at any time to impinge on your reputation or character. Please bear that in mind. A. Thank you, sir.

Q. We are only dealing—— [81]

A. If my sister would not have moved into the property, the property would have been the property of the trust. But since my sister moved in, counsel advised, "No, that you can't do that, that somebody may say you are buying the property so your sister could live in it, with trust money." So we wiped the deal out quick.

(Testimony of Jack Edward Smith.)

The Court: In other words, he actually invested in it?

The Witness: Yes. The property is still there, your Honor, on mine and my wife's name, I believe, and one of my relatives live in it, and that's why my counsel advised that deal is not suitable for trusts.

The Court: I see. You are not responsible to anybody because you did not create a guardianship for the children, under which you would have to account every year to the court, and the court would pass——

The Witness: But we can't——

The Court: Just a moment. (Continuing) ——and the court could pass on your acts, and determine whether you used the money wisely or not. So why were you worried about somebody taking money out of the trust for one purpose or another?

The Witness: For exactly the reason that there may come up something like that, that some day it might come up, and you might say, "Now, Jack, you are not running that trust legitimately." We didn't know anything about it.

The Court: They have no right under this trust, the way [82] you have drawn it.

The Witness: No, your Honor,——

The Court: Supposing tomorrow you take all this money and put it in a venture, and lose it the day after. Under this trust you have no responsibility.

The Witness: Your Honor, I went to the best——

(Testimony of Jack Edward Smith.)

The Court: No court could make you put it back, because you are not responsible to anybody.

The Witness: Your Honor, I went to the best counsel I knew.

The Court: That isn't the point. I am trying to find out.

The Witness: You must take the reasons. I am a layman, and you are a very brilliant lawyer.

The Court: No, we have to look back at your own method of thinking. Why should you be afraid of being tripped up by somebody when there were no limitations.

The Witness: We never thought——

The Court: Your son couldn't bring you into court under that trust, and make you account for anything, because your answer would be, "Everything that is there I gave him, and we made the trusts, and we are not accountable to anybody."

The Witness: Well, we didn't feel that way, your Honor.

The Court: I am talking legally.

The Witness: We didn't feel that way. Well, I didn't know the legal point. [83]

The Court: That is right. If you wanted to do it——

The Witness: I thought we were legally bound to be very careful.

The Court: If you wanted to do it, you could have done as they did in the Schlobohn case,—wasn't that it?

Mr. Hochman: Yes.

(Testimony of Jack Edward Smith.)

The Court: They went to the state court and had the court appoint them trustees, and they accounted every year to the court.

The Witness: We didn't think that was necessary, your Honor.

The Court: I see. All right.

The Witness: And it was run pretty well without it.

The Court: Your intentions are strictly honorable so far as your children are concerned, and nobody is disputing that. Mr. Hochman does not dispute it.

The Witness: That is what every taxman says.

The Court: Some of us wish we could exercise similar generosity to our own. Unfortunately, you cannot do it on a judge's salary.

Mr. Hochman: It was the Schlobohn case, your Honor.

The Court: That is why your son might be wiser if he got into the shoe business. I thought I would just introduce a little lightness into this litigation. We are getting too serious. [84]

The Witness: That's right.

The Court: Don't misjudge any of us. Mr. Hochman said nobody is doubting your integrity. This is just a legal proposition.

The Witness: I understand that, sir.

The Court: We have to inquire into the circumstances because the law says there are certain earmarks by which you can determine whether a trust is good or not. You heard me say this morning that

(Testimony of Jack Edward Smith.)

I have had them on both sides, and some I have ruled are good, and some bad, and it all depends on the same principles. Each case has to be judged by the particular facts, and if we are probing into these things, it is merely because it is our duty to do it, you see, in order to find out whether this arrangement is of a character that the law recognizes as valid or not. It does not go to motive at all. It goes more to intent.

The Witness: By the same token, your Honor, we didn't do anything that we didn't ask for advice on that it was absolutely right.

The Court: Certainly.

Q. (By Mr. Hochman): Mr. Smith, is it correct that as of the end of 1948 the schedules that we have before us, Plaintiffs' Exhibits 20 and 21, reflect that the Barbara trust and the Howard trust do not own any real property; is that correct, sir? [85]

A. They don't own any real property, no.

Q. Now, I believe, Mr. Smith, you stated that the motive you had for the formation of these trusts was to protect your children, and give them security. A. That's right.

Q. You mentioned, too, sir, that you had discussed the matter of a will with your attorney, and I ask you, sir, whether or not you knew that you could by way of will leave your property to your children? Did you know you could do it by will?

A. Yes, I know. I had a will drawn, but we wanted to take and to set something up prior to the

(Testimony of Jack Edward Smith.)

will, prior to I die, to give something when I am alive.

Q. Now, then, the money in terms of the three certificates of indebtedness, the United States bonds, if you will, and the notes of your wife that were returned to the business,—the securities, therefore, of the children were back in the business?

A. The business was good, sir; good security.

Q. Well, let's look at it this way: Before the trust the children, in terms of any substantial inheritance, and I don't want to be morbid, but we must face these things, would depend upon the welfare of the Boston Shoe Company; is that correct?

A. I didn't get your question. Make it simpler.

Q. Before you had the trust arrangements,——

A. Yes.

Q. Before you had that, you owned the Boston Shoe Company, and your children had very little.

A. That's right.

Q. They were very young, and had very little.

A. That's right.

Q. Now, then, after the windfall that they would get upon your death at some date, we trust very long in the future, would depend on how well the Boston Shoe Company was doing; is that correct, sir? A. Right today?

Q. Well,—— A. Or on that date?

Q. Perhaps my question is confusing. Let's go at it this way, if we may: Forget for the moment that any trust arrangement was made. Forget for

(Testimony of Jack Edward Smith.)

the moment that they are partners. Let's assume that you owned the business, and none of this had been entered into. Now, then, whatever security in the future your children were to get upon, say, your death in terms of inheritance would depend, would it not, on how well the Boston Shoe Company had been doing, and was doing at this projected time in the future; is that correct?

A. No, it is not absolutely correct, sir.

The Court: I don't think you get the point. [87]

Mr. Hochman: No, your Honor.

The Witness: I am, your Honor, because it would depend on how much Mrs. Smith wanted to give the children.

The Court: That is not the point. The point is this: If you wanted to give them security, you see, why not give them something aside from the business, something that supposing you went broke, they would still have had it. If the Boston Shoe Company went broke, they would have nothing.

The Witness: That was our clear intentions, but about that time we started to make the arrangements, and until Mr. Gittelson finished it, it took over a year and a half.

The Court: I see. And it was determined that this was the best thing, this tie-in?

The Witness: That was the advice of Mr. Lippman, Mr. Arnold of the Union Bank, Mr. Cameron, Mr. J. B. Lewis, and if Mr. Lippman was still alive, and Mr. Siegel will perhaps remember that, we consulted with these people, and they all talked

(Testimony of Jack Edward Smith.)

that I am in the shoe business, and I know the shoe business, and Mr. Finkle perhaps, and everybody felt that would be the best security for our children. Our business has been a business with a profit record in every year since we started. There has never been a year without a profit, and a fair profit.

The Court: But it is true that your creditors could not touch this trust. I assume they couldn't. I don't know. [88] The creditors could not touch the trust, but you yourself could.

The Witness: The creditors could touch the trust because the trust was a part of the investment in the business. They could touch the Boston Shoe Company.

The Court: They could not touch the money in the children's account.

The Witness: I don't quite understand you.

The Court: A creditor of the Boston Shoe Company?

The Witness: A creditor of the Boston Shoe Company can get—he could get at it. In my opinion, he could, because it is an investment in the Boston Shoe Company. My opinion is that he could.

Mr. Lund: It is not a limited partnership, your Honor.

The Court: How is that?

Mr. Lund: It is not a limited partnership.

The Court: That is right. I was thinking in terms of a limited partnership. Yes, the private estate could be used.

(Testimony of Jack Edward Smith.)

Now, that makes the question Mr. Hochman asked even more pertinent, because if, as you understand, this trust was not protected even against creditors, and it was not protected against what you might want to do with it by drawing it out, if you chose to draw it out, what advantage was there for the children in tying it to your business rather than putting it [89] into something so that if something should happen to your business they would still have something, which you say was your intention.

The Witness: Your Honor, we went around looking for several investments, and outside of government bonds at that time, which were paying a high interest, there was nothing else to do, as far as I was concerned, to do with the money.

To give you an idea, we looked at a certain piece of property, and they asked $40,000.00 for it at the beginning of 1942, and at the beginning of 1943 they asked $75,000.00. That was right next door from where I am, and it finally was sold for $110,000.00. It is quite a story, and every time I went to the agent he asked $20,000.00 more.

The Court: It seems to me that that would have been an inducement if that happened to the price. Of course, we know what has happened. We have tried many condemnation cases.

The Witness: We quarreled every time we talked about the deal. Finally we got sick and tired of it. Every time we talked to him, it was $20,000.00 more.

The Court: Maybe you should have bought it,

(Testimony of Jack Edward Smith.)

and sold it and taken your profit, and put it into government bonds.

The Witness: Well, we didn't do it. I mean, it is past judgment, it is hind judgment.

The Court: All right, Mr. Hochman.

Mr. Hochman: Thank you, sir. [90]

The Court: I have tried to get an answer to that question, and I think we have got it in an indirect fashion.

Mr. Hochman: Thank you, your Honor.

Q. (By Mr. Hochman): Mr. Smith, I believe your testimony a short time ago was that regarding the business you needed the money back in the business; is that correct? Is that what you said, sir?

A. Yes, I felt that by having the money in the business I would have a larger and stronger company. You must know that at that time the majority of the dealings, the transactions, were made on cash. The manufacturers sold the guy that gave him the money.

Q. I appreciate that.

A. You may find some places where they gave people money in advance.

The Court: But you didn't get any money. All you got was canceled notes.

The Witness: Your Honor, we did.

Mr. Hochman: No, your Honor. May it please the court: Returned were these three United States certificates of indebtedness, and those surely, I think the court will acknowledge, could be transferred into cash quite readily.

(Testimony of Jack Edward Smith.)

The Court: Oh, I see.

Mr. Hochman: So as to one of the trusts, it is quite true we may term it cash returned. [91]

The Witness: Your Honor, it made a terrific difference in our credit standing. So long as we took the $100,000.00 notes from Mrs. Smith back in the business, and showed them as a liability, it made a terrific difference in our rating and our credit.

The Court: On paper.

The Witness: Well, that is how business goes. It is all paper.

The Court: I noticed on the back of them she didn't cancel the notes. She merely endorsed them over to you.

The Witness: Your Honor, we send out thousands of cases of shoes per week, and all we get is T.A.'s and paper. You don't see much cash. That's how business is done.

Q. (By Mr. Hochman): However, the $30,000.00, the three $10,000.00 United States certificates of indebtedness, those were what you had given, is it not right, to one of the trusts on September 29th, and they returned it October 1st to the business.

A. Officially as of September 29th, but it was planned quite a long time ago. It was set away quite a while ago.

Q. But in terms of your legal rights, you did not relinquish them until September 29th, and you got them back for the purpose of the business on October 1st.

A. Legally, of course, you can say that, that is

(Testimony of Jack Edward Smith.)

right. If Mr. Gittelson wanted to date them back, he could perhaps [92] have dated them back, but the money was set up a long time before that.

Mr. Hochman: So in this respect, may it please the court, I might perhaps not have advised the court of the proper facts on the $30,000.00 of these bonds. They left Mr. Smith's hands on the 29th of September, 1943, by way of becoming the corpus of one of the trusts, and returned to the business of the Boston Shoe Company on October 1st.

The Court: That is right.

Mr. Hochman: So it had left it for a period of three days.

The Court: All right.

Q. (By Mr. Hochman): But it is true that what was given to the Boston Shoe Company or to yourself for the 15 per cent interest of the other trust was one of your own notes that you had previously given your wife.

A. That's right. It reduced that liability.

Q. I think it would be fair, Mr. Smith, would it not, to say there was no fresh capital added by the children?

A. I don't know what you talk about by "fresh."

The Court: Outside money. Let's call it outside money.

The Witness: Your Honor, this is not disputable. I mean, you understand all of these things. We wanted to give something to our own kids, and had we bought——

Q. (By Mr. Hochman): Mr. Smith, it is an ad-

(Testimony of Jack Edward Smith.)

mirable [93] situation, but we are dealing here with rather unemotional facts.

A. Had we gone out and bought real estate, you fellows probably wouldn't be here, and I would never have seen a "T" man in '46. You wouldn't have made out—we had all good intentions, and because we invested into something a little more lucrative, you know, you are all complaining about it.

Mr. Hochman: No, sir. It has to do with coming back to you.

The Witness: Everything,—we never touched——

Mr. Lund: Mr. Smith, wait until you are asked questions.

The Court: Well, it is argumentative.

The Witness: Yes.

Mr. Lund: That is right.

The Witness: I don't mean to argue, your Honor.

The Court: There is nothing personal in any of these inquiries by Mr. Hochman.

The Witness: I know there aren't.

The Court: It is merely a desire to get the basic facts in this transaction.

Mr. Lund: I might remind the witness that his counsel will make the proper argument at the proper time.

The Witness: Well, your Honor, you know you are human up to a certain extent.

Q. (By Mr. Hochman): Mr. Smith, does the Boston Shoe [94] Company manufacture any shoes?

A. No, not now.

(Testimony of Jack Edward Smith.)

Q. It is, then, what we may term perhaps a brokerage? A. It is a wholesale firm.

Q. Do you buy from a manufacturer and sell to the retailer?

A. That's right. Not brokerage. It is wholesalers. We are dealers. We buy and sell.

Q. How many people during the period of 1942 to 1948, inclusive, and perhaps as far back as 1935, —about how many people were working for you?

A. At any one time?

Q. Yes.

A. I think between 20 and 25 at one time. I don't remember right out. I can check that.

Q. Well, approximately.

The Court: Were they all located in the plant, or did you have people on the road?

The Witness: We had people on the road. We travel about five or six.

The Court: And they call on the trade?

The Witness: Yes.

The Court: Like the Hoffman Hardware Company, for instance? They used to be your neighbors there on your street. [95]

The Witness: Yes. Like Los Angeles Street people do. We all do the same thing.

The Court: The Hoffman Hardware Company has moved away from there now, but they have people who go out and call on people in the hardware trade, and all this firm does is fill orders.

The Witness: No, we buy the shoes.

The Court: That is right.

(Testimony of Jack Edward Smith.)

The Witness: We buy and sell them, and put our name on them.

The Court: And sell them to customers?

The Witness: Sell them to customers.

The Court: And some of them come direct, and some are solicited by your salesmen.

The Witness: By our salesmen, that is right, sir.

Q. (By Mr. Hochman): You mentioned earlier, Mr. Smith, that on occasions you would make seven or eight trips back to the east. Would that be for the purpose of purchasing merchandise?

A. Yes, sir.

Q. And were you the one who took the trips back east usually?

A. Mr. Weishaupt used to go with me before he was a partner. I think he went a couple of times himself. I don't remember exactly, but Mr. Weishaupt would go with me, and [96] sometimes we had a buyer in the market.

Q. Now, isn't it true, Mr. Smith, according to your partnership agreement and according to your own operation and understanding of it, that no major decision regarding the Boston Shoe Company could be made without your consent? Is that a fair statement, sir?

Mr. Lund: We object to that. We think the document must speak for itself, your Honor.

The Court: I think, regardless of documents, the operation in practice is important, and that can only be determined by what was actually done. I think the question is pertinent.

(Testimony of Jack Edward Smith.)

The Witness: Your Honor, what does he call a major decision?

The Court: Well, any decision on account of or on the conduct of the business.

Mr. Hochman: Important.

The Court: You never took a vote with your wife or children to decide by a majority vote what you were going to do?

The Witness: Oh, with my wife, yes, I would discuss certain things.

The Court: You would discuss it with her?

The Witness: Yes.

The Court: But with the children? [97]

The Witness: With the children, no.

The Court: So whatever you and your wife decided had to bind the children?

The Witness: That's right, yes.

The Court: Because there was no third independent person representing them. You represented them, too, because you were the trustee.

The Witness: That's right, yes; with the exception of the employees that might make a major decision.

The Court: But you employed them?

The Witness: We hired them, yes.

The Court: So they were not consulted.

The Witness: No.

The Court: Or anybody representing them?

The Witness: Oh, well, sometimes——

The Court: That is what he means.

The Witness: Oh, sometimes they were con-

(Testimony of Jack Edward Smith.)

sulted. Howard has been consulted about a lot of things.

The Court: Well, a wise man always consults trusted employees, you know. Otherwise, if you don't learn to delegate some of your duties, you cannot be a success in any business.

The Witness: That is right.

The Court: You have to learn to delegate some of your duties. [98]

The Witness: That's right.

The Court: You yourself say that the business ran itself pretty well when you were sick?

The Witness: That's right, yes.

The Court: That shows you have it organized well.

Mr. Hochman: I have no further questions, your Honor.

The Court: All right.

Mr. Lund: Just a few very brief ones.

Redirect Examination

Q. (By Mr. Lund): Mr. Smith, the Ben Breiman that has been referred to, is that the same as Ben Breiman Smith? A. Yes, sir, the same.

Q. The same individual? A. Yes, sir.

Q. From the time that these two trusts were set up in 1943, and for the years thereafter, Mr. Gittelson advised you in connection with the affairs of the trusts?

A. That's right; Mr. Gittelson, and Mr. Finkle, and sometimes some others.

(Testimony of Jack Edward Smith.)

Q. Did you understand from Mr. Gittelson that you and Mrs. Smith, as trustees were responsible and accountable to the children for your conduct in the handling of the affairs of those trusts?

A. That's right. [99]

Mr. Hochman: Your Honor, I object. That is quite a leading question.

The Court: That is all right.

Mr. Hochman: I think it even gives the answer to the question.

The Court: That is all right. So long as I allowed the other one, I will have to allow this one, to be consistent. I don't think they are responsible. I don't think any court could touch the trusts.

Mr. Lund: I don't know whether the witness has answered, your Honor, but we will want to have the opportunity to try to convince your Honor to the contrary. We think you are mistaken in your interpretation of the legal effect of this trust agreement. We do want to pursue that, and we have some authorities on that.

The Court: All right.

Mr. Lund: Did we get an answer to the question?

The Witness: Yes, sir.

(The answer was read.)

Mr. Lund: That is all.

(Witness excused.)

The Court: All right. Is that all?

Mr. Lund: We rest, your Honor.

The Court: Is there anything that the Government desires to present? [100]

Mr. Hochman: No, your Honor, the Government has no witnesses.

The Court: Gentlemen, we will take a recess, and then I will hear any argument you desire to make.

Mr. Lund: Your Honor, if we may, we would like to have the opportunity, even if it is only a short period of time, to file a brief.

The Court: No, I don't require any brief in cases of this character. I want oral argument, because we all know the cases, the Tower case, the Culbertson case, and the other one, and I have written opinions myself. If I want any legal authorities after that, I will ask for it.

Mr. Lund: We do appreciate that on the family partnership points, and we don't want to burden you with that type of argument, but we are disturbed about your Honor's interpretation of the legal obligations in the trusts.

The Court: If you can show me that under the law of California anybody could invest in that trust, why, I would like to have you tell me.

Mr. Lund: We are, frankly, not prepared with authorities on it, because we did not anticipate it.

The Court: It does not make any difference because I think there is nothing to limit him in drawing it all out and spending it.

Mr. Lund: For purposes other than trust purposes? [101]

The Court: For the purpose of investing it and losing it. He is not an executor.

Mr. Lund: He is subject to the exercise of due care as a trustee, your Honor.

The Court: That is true. So are the banks. In other words, I take this, and I am making this statement so that you can argue to the contrary. This trust is so broad, it is like the bank trusts, and if he went and invested in a stock, and it went to nothing, you would have no recourse on him unless you could show that he did it to defraud the trust, and you can't do it. That is what I meant.

I meant that he could use the worst judgment in the world, and lose the money, and the children would have no recourse.

The only reason I was bringing that out is because in some of the cases, or, I think in one of the cases the father, to protect himself, had had a court appoint a trustee, and even in that case it developed that the trustee always gave his consent. That is the reason why I was asking those questions, and I will hear you on the subject. Perhaps I am reading it a little more broadly than you are.

(A short recess.)

Argument on Behalf of Plaintiffs by Mr. Diehl

The Court: All right, Mr. Lund, you are the plaintiff, so I will hear you first. [102]

Mr. Diehl: May it please the court: Diehl speaking for the plaintiff.

The Court: Mr. Diehl, all right.

Mr. Diehl: I believe it can be said that the good faith of the parties in this matter cannot be questioned. They truly intended to set up an estate for their children, and I think it can be truthfully said also that the theoretical saving of income taxes, if it can be called that in any event, was not the motive behind it; that they truly wanted to give something to their children, and the taxes would fall where they might.

If we can assume that the good faith was there, then the question, it seems to me, is only what did they do, and what was actually accomplished?

Now, there has been quite a bit of confusion, I think, over the subject of what gifts went to whom, and how it got from the parents to the trusts, and from the trusts back to the father.

The Court: The reason is there was no lapse of time.

Mr. Diehl: That is true. I think for our purposes——

The Court: It is just like a paper transaction.

Mr. Diehl: For our purposes, I would think we could treat this as a gift of an interest in the business to the children, with the result of a resulting partnership being set up. [103]

But bear in mind, before we go into that any further, that prior to the time this transaction was actually consummated, between September 29 and October 1, 1943, plans had been under consideration, and, in fact, a gift of $4,000.00 cash to each child had been made towards the end of 1942 as the beginnings of a fund.

The parents had under consideration very definitely the possibility of acquiring real estate outside of the Boston Shoe Company for the benefit of the children.

It was only after giving due consideration to the other possible investments that the decision was finally made that the best place for the children's interest was in the Boston Shoe Company, which was up to that time operated as an individual proprietorship by the plaintiff, Mr. Smith. It was a business that he knew. It was a prosperous business, and it was one in which he was sure that the children's capital could be increased substantially over the years, and a lot faster than it could if it were invested in simple income-producing properties, or bonds, or other investments.

Therefore, the decision that was finally made was to put them in as partners.

Now, at that point it seems to me that it is unimportant whether they were giving a government bond and a note, respectively, and then turning around and trading those back for an interest in the business. At that point what it amounted to [104] was that the mother and father, respectively, made gifts of parts of their interest.

The Court: May I interrupt?

Mr. Diehl: Yes, you may.

The Court: I want to say this: I take it that the Culbertson case modifies the Tower case to the extent of holding that the providence of the fund is in itself not determinative, that is, the fact that the money put in was actually a gift to the children

would not determine the matter. In other words, as to the Culbertson case, the portion that the Government cited in its brief is one that we have used dozens of times. It says:

"The question is not whether the services or capital contributed by a partner are of sufficient importance to meet some objective standard supposedly established by the Tower case, but whether, considering all the facts—the agreement, the conduct of the parties in execution of its provisions, their statements, the testimony of disinterested persons, the relationship of the parties, their respective abilities and capital contributions, the actual control of income and the purposes for which it is used, and any other facts throwing light on their true intent—the parties in good faith and acting with a business purpose intended to join together in the present conduct of the enterprise." [105]

So that the fact that the initial capital was a gift to the children would not in itself determine the matter. You would have to go into those other elements. In fact, in some of the other cases I have taken that statement and broken it down into six or seven elements. I have forgotten in which of the opinions that I wrote I did that. But you have to consider it. There is also one feature of this case which makes it a little different from the others, the very feature that I pointed to, with Mr. Smith wondering why I was doing it, the fact that the money was left there.

In other words, there is no shifting of income, such as sometimes appears where the parents, after

making the gifts, give themselves the right to do as they please with the income. And while, as I say, they have a perfect right to do that, the way I interpret it, there is no showing that they ever used it. In fact, they didn't even draw money for the education of the children.

So that that is an element which often is not present in other trusts of this kind, because there is some kind of a siphoning off of the income, whether for the maintenance of the children, or otherwise, you see, and that is not present here.

Mr. Diehl: Yes. And, if your Honor please, of course, you have already mentioned yourself the fact that the trusts [106] do have something in them that belong to the trusts and to the children.

The Court: That is right. Of course, there is one other matter, there is no question but what control remained solely in the husband, and the business was conducted afterwards just as it had been before, as far as seeking business advice of anyone else, and regardless of what the papers said, he made the business, he created it, it was his before marriage, and thereafter, when he took his wife in and later the children, he continued to be the managing partner to whose ability the success of the business was traceable.

As a matter of fact, Mrs. Smith herself said one of the reasons for bringing the children in was the realization that he made a success of it, and they felt he would continue to do so, and he evidently has.

Mr. Diehl: Yes. I would at that point like to

remind your Honor of the statements made by the Ninth Circuit in the Toor case that control for one's own benefit and control as a fiduciary for the benefit of someone else are two different things, and while it is true that he was the managing partner, he still had to think not only of himself, but of his fiduciary duties to the trusts, and to his other partner, Mrs. Smith.

I would also point out that after——

The Court: That was my case. [107]

Mr. Diehl: Yes, that was your case.

The Court: But in the Toor case there was a guardianship created in the state court, and he was accountable. If you read my opinion, you will find he rendered accounts.

Well, I don't know whether it was in that one, or in one of the others.

Mr. Diehl: The Toor case involved a trust which at first was not an irrevocable trust, and it was changed to an irrevocable trust a year or so after the partnership was formed.

In our case, of course, both trusts are irrevocable, and the trustee, we still insist, has responsibilties that he cannot avoid. He cannot use the trust assets as he sees fit except for the benefit of the trust itself.

Now, true, he can use his discretion, and he is not responsible if he exercises bad judgment. But that is the case in practically any trust that is set up these days. The trustee is still, though, responsible for the proper administration of that trust. And today, if the son discovered that his father had mis-

appropriated the trust funds, he could certainly bring an action against him and recover for his defalcation.

The Court: I have no doubt. I mean short of actual fraud.

Mr. Diehl: But I submit that the trusts are genuine [108] and cannot just be called mere paper trusts, and ignore them; that they are genuine estates for the benefit of the children.

As such, they do actually own an interest in the business through the partnership. They not only own the interest, but they have derived benefits from the interest, in that distributions have been made, which have been invested in government securities and have been deposited in the building savings and loan accounts, so that the trusts do have a substantial amount in them over and above the investment in the partnership, and which they would not have had without their participation in the partnership.

The Court: All right.

Mr. Diehl: I would like also to point out as at least an indication that this definitely was not a tax device, that, in the first place, the trusts were given relatively minor interests in the partnership. If the splitting of income had been the prime motive, there would have been no reason why they shouldn't have made a four-way split, or an even split, instead of giving them only 15 per cent. Also, that the services of the parents, that the father and mother rendered to the partnership, were recognized, so that they were given salary allowances, so that the distribut-

able income represented properly a return on the capital invested, so that the father and mother were not dividing with their [109] children the income attributable to their personal services, all of which is to their credit.

As a matter of the careful administration of the trust, I would point out the testimony concerning the loan, and the proposed purchase of the property by the trust, and their deciding not to go through with it for the trust when it turned out to be a family affair. In other words, they are not using the trust funds for the benefit of any member of the family.

So with that point, if the court please, on the basis of the good faith of the parties and the actual carrying out of their intentions, and actually conveying something to the trust which is real, it demonstrates that something was actually accomplished, and it should be recognized for tax purposes.

Now, one more point I should make which was brought up by the defendant's brief: There were two partnerships here, and two partnership agreements. One ran from October 1, 1943, to December 31, 1944. The other ran from January 1, 1945, to June 30, 1948. The second one included a complete stranger, one Herman Weishaupt. He joined in the partnership with all of these people and recognized all of them as partners.

Furthermore, there were definite changes in the powers of the plaintiff, Jack Smith, when the second partnership came long. [110]

There is nothing in that agreement which is un-

usual to any ordinary partnership. It is all based upon the decisions of the partners, and in that partnership Jack Smith was not a majority—did not control a majority interest in the business. He, as an individual, owned 36 per cent, and he, as the trustee, owned 13½ per cent, which was only 49½ per cent. Mrs. Smith and Mr. Weishaupt could overrule Mr. Smith under that partnership, so that his control was definitely restricted in that case.

It is our earnest belief that in this case judgment should be entered for the plaintiffs.

The Court: All right, Mr. Hochman.

Argument on Behalf of Defendant by Mr. Hochman

Mr. Hochman: May it please the court: The Government takes issue with plaintiffs' contention as to good faith. By this the Government does not mean that the people do not have good faith, but, rather, we are confining ourselves to the income tax law, and the law before this court. We speak, then, of the good faith of the Culbertson case, to join together with a business purpose in the present conduct of an enterprise.

While it is true under the Culbertson case, your Honor, that the source of capital is not a determining factor in and of itself, yet it is an important factor, because if it is present, and fresh capital is present, under the criteria [111] of the cases emanating from the Culbertson doctrine, the proposition of the plaintiffs could stand.

In the present case, in the case at bar, however, there is no capital originating from the children.

From the testimony and the documents it is clear that all the money, or the notes and the bonds, were derived from the Boston Shoe Company and the parents, Mr. and Mrs. Smith.

Now, then, relative to this matter of control, your Honor, the cases before this honorable court, the Schlobohn case, the Toor case—which, incidentally, had an independent guardian, an independent trustee—and many, many other cases rest on this ground of good faith. Good faith, then, is measured by the yardstick of control.

As recent as March 1954 the Tax Court overturned a situation where a father had set up an independent trustee, but that independent trustee was in his employ, and the Tax Court then pointed out that that is the same thing as the man retaining control by becoming the trustee himself. You simply have no division of control interest.

You have what you started out with: In this case Mr. Smith running the Boston Shoe Company. Under the first partnership agreement he had a tremendous amount of power. No decision could be made without him, and then, too, the amount of salaries could be controlled by Jack and Mrs. Smith.

Counsel has made the point—— [112]

The Court: Of course, that merely stems from the fact that he owned the control.

Mr. Hochman: In part true, your Honor, but it is interesting in terms of determining how much——

The Court: You know the old question they used to ask, and the answer given to the conundrum, "What is the difference between 51 per cent and

49 per cent?" And the answer is, "100 per cent." In other words, that little two per cent that gives a man control is worth 100 per cent.

Of course, the thing got so bad, however, that the court devised the equitable doctrine that in the case of corporations they would protect the stockholders, even against what the majority stockholders would do, by devising equitable principles.

So that control was derived from the fact that he and his wife owned the control of the business.

There is no question in my mind that after this partnership was entered into Mr. Smith continued to control the business just as he had before. But when these cases speak of control, they speak of control, when you are dealing with a trust, of the funds, and here, regardless of what the papers said, it is quite evidence that the income derived from the partnership was distributed to the children regularly, and remained there, and was not siphoned off in any fashion.

Mr. Hochman: Your Honor, there is a substantial question—— [113]

The Court: To that extent the case is a little different from some of the others, because in reality, through the high sense of honor—and I say that sincerely—the high sense of honor that the parents had, they felt, although, as I say, I think they could have squandered the money if they wanted to, but with the high sense of honor they had, they did not take out of the trust funds even the legitimate expenditures for the children's education, which any court would allow them to do.

Mr. Hochman: This, your Honor, is commendable, but then in the nature of this suit the Government is being sued to contribute to the trusts by the prayer for relief.

The Court: Of course, if the partnership was merely a device to avoid the surtax, the fact that an arrangement reduced one's tax incidence is not the criterion. It has always been the theory of the Government, or the theory of the courts that a man may choose any method he desires for the purpose of carrying on his business, but once he chooses it, he is bound by it. If he chooses one that reduces his taxation, the loss that might result to the Government cannot stand in the way of giving it recognition.

In the F. Hugh Herbert case, which involved collapsible corporations, I went very thoroughly into the study of that problem, because it had become the custom of Government counsel to criticize these devices, and I pointed to the [114] fact that from the very inception of the income tax legislation, which followed the adoption of the amendment in 1913, the courts had held,—and even before that, when the first wartime revenue statute was passed during the Civil War, the courts held that a person could transact business in such a manner so as to avoid tax. The case arose in a criminal case where they prosecuted a bank because they claimed they resorted to a certain method of pooling their accounts, resorted to certain business methods of pooling their accounts for the purpose of avoiding the stamp tax passed during the war.

The court reversed the conviction and held it was perfectly legitimate for them to do so.

The thing that vitiates a partnership of this character is the fact, if it be a fact, that the tax saving is the sole motivation of the arrangement, and none of these elements which the court enumerates in the Culbertson case, the portion I have quoted from your brief, is present.

So in many of these cases the Government offers nothing because it has nothing to offer.

In any one of these cases I have tried, the Schlobohn case, the Toor case, and one or two others that went up on appeal, or in all of them reliance was made upon certain facts brought out in the examination and cross examination of the parties themselves, in order to determine whether the partnership or the interest given to the children was [115] legitimate for tax purposes.

In many cases we start with the assumption that it may be perfectly legitimate under the law of the particular state, and that is a matter that we run into in taxation all the time.

I remember one of the first tax cases I tried early in my career as a judge, and which I tried in the Western District of Washington. It is known as the Wenatchee Bottling Works case. That involved the payment by the men to themselves of large salaries, and making the salaries retroactive some nine or ten months. They were arguing that it was perfectly legitimate under the law of Washington to do that, and I said that it was perfectly legitimate under the law of Washington, but the Government has a right

to question whether that is a reasonable deductible expense, and in that particular case I reached the conclusion that it was not.

So in many of these cases the Government is in the peculiar position of being allowed to question a transaction that is perfectly legal. Some of them the courts have granted, and some they haven't.

For instance, we consider that when property is held in joint tenancy, as it is in California, that on the death of the spouse all you have got to do is to bring an action to establish death, and in the past we didn't even have to do that, until the section was amended, and you will remember [116] the lawyers had that amended. In the past all you had to do was to go to the Title Company and file an affidavit of death, and they would change it.

Nevertheless, the Government does not choose to recognize it, and they consider it a taxable incident. Even before it was put into the statute, it has always been in the regulations. They merely say, "That is all right for state purposes, but I am going to hold that transaction a taxable transaction."

What I am trying to say is that you may start with legality, and still reach the conclusion that for taxation purposes the legality does not solve the problem, because if legality were the sole criterion, the Government would lose out in many of these cases, because all you would have to do would be to determine whether what the taxpayer did was legally proper under the laws of the state where he did business.

All right, go ahead. My object in making these comments and observations is to clarify my thoughts. Many lawyers who have practiced before me, and I have been a judge for 26 years now, both in the state court and here, know that I have a practice of telling you what is in my mind. The reason I prefer oral argument is that I have a saying, "I can argue with a man who is about to write a brief, but I can't argue with the brief in my chambers, and if you deliver an oral argument, I can ask questions and give you an opportunity to [117] overcome any misimpression I may have in my mind either as to the law or as to the facts."

Now, no one has a right to take a vested interest in what I say, and I am making this statement to you because you are new in the Court House, at least, so far as I remember, this is your first apperance before me in any case. You may have sat in with Frank Mahoney, or Harpole, or Mitchell, or some of the other men, but so far as I am concerned, I think it is your first appearance here, and I just wanted to tell you what the meaning of this inquiry is.

Mr. Hochman: I thank the court.

Your Honor, these cases, the Schallerer case in the Seventh Circuit, the Feldman in the Fourth Circuit, the Toor case in the Ninth Circuit, the Boyd case in the Third Circuit, all of these cases, your Honor please, concur with what you have just said here, have just finished saying, and reflect in terms of the intent required for income tax purposes and confine it just to that question.

The Court: You see, the problem the courts have, however, is an easier one from the problem we have. In the Toor case the question was whether my conclusions were correct or clearly erroneous. And I don't know of any case where the higher courts have reversed the trial judge, whether he has reached one conclusion or another. My problem is more difficult than theirs. I have got to draw the inference that they [118] say I should draw, and then after I have drawn it, all they have to say is, "If it is not clearly erroneous, I will sustain it, because that is what the rules say."

Mr. Hochman: Your Honor, in the Schlobohn case, which was not appealed from this honorable court, the Government's contention, which your Honor upheld, was that this bona fide business purpose which was necessary was negated by the control exercised by the plaintiff in that case, and that is the way the case turned, on that issue. Now, then, whether or not——

The Court: I have forgotten whether that is the one, but he had a different control. That is the case where he had a guardian appointed, and then he went before the court and had his percentage increased, and he did all sorts of things. Then he had the power to terminate it in five years, I think, and he actually terminated it. He had great powers in exercising it in a manner that does not appear in this case. I think I am correct in that.

Mr. Hochman: If we may point out to the court, what is done with the money afterwards, in any event, is not determinative of the initial question

of what criteria we adopt, and how we measure the criteria of control.

What I mean to say, your Honor, is this: What happens to the money once it goes to the trust is not of import. A man may have all the donative intent in the world, a man may [119] desire with all his heart and soul to assign part of his income forever and irrevocably to his son, and do so, but that assignment of income for tax purposes is not recognized, although the gift, as such, under state law would be complete.

And so the fact that these parents were doubly generous in terms of not taking the money from the trusts for the education and welfare of the beneficiaries of the trust does not mean that the money that went into the trust should not be taxed to them, and I think it would be to confound the issue to go beyond that first stage.

We are considering, if the court please, the money that is going into the trust as opposed to what is done with it once it is there, and to that end, your Honor, we feel the Government contends that the control issue is determinative, that the testimony and the documents reflect, in accordance with case law and the cases decided before this honorable court, that the plaintiffs have not met their burden of proof in this case in overturning the ruling of the Commissioner as to the recognition of this trust partnership relationship for income tax purposes.

Mr. Lund: May I have just a brief reply, your Honor?

The Court: Oh, yes, you are entitled to the opening and the close. You are the plaintiffs. [120]

Closing Argument on Behalf of Plaintiffs by Mr. Lund

Mr. Lund: First I hesitate to keep differing with your Honor about the effect of this trust agreement on the right of the parties to use it for support, and so on.

The Court: Mark you, I have not had an opportunity to read them in detail, as I have told you.

Mr. Lund: You have not. I did want to point out that each of the trust agreements merely provides that the income is to be accumulated, and there is nothing to be expended from the trusts prior to the age of 25, when a certain part could be distributed to the two children.

Between the ages of 21 and 25, however, for purposes of support and education, and anything of that character, the trustee could make distributions to the children from the trusts with certain formulas limiting the amount that could be distributed between the ages of 21 and 25. But up to that age the trustees could not, without rendering themselves liable to the beneficiaries, use the trust funds for any purpose other than for accumulation, paying of expenses, and so forth, and proper investments.

I think, and I gather from your Honor's analysis, oral analysis of the cases, and so on, that we are trying to state the issues as simply as we can, and I suppose the question boils down to: Were the trusts created and the partnerships created for the

purpose of reducing the income taxes of Mr. [121] and Mrs. Smith?

I believe, your Honor, that the evidence in this case is actually very strong and very conclusive that income tax considerations had no part in the determinations to create the trusts or the partnership with the trusts as partners.

Now, counsel for the Government has referred, as properly he should, to this element of control. However, that matter is not determinative. It is one of the factors to be taken into account, and it is obviously true that Mr. Smith, with all his years of experience that he has had in the business, Mrs. Smith, if she felt otherwise, or Mr. Weishaupt, the other partner of later years, would not be very apt to try to force their judgment upon him in view of his great experience, but the fact of the matter is that from 1945 and on, beginning in January of 1945, so far as his legal control was concerned, Mr. Smith did not have it. He did not have a 51 per cent interest in the partnership. He had a 49½ per cent interest, considering his interest and his interest as a trustee.

So whatever merit the legal control this individual may have had, whatever value of importance it has in the Government's case, from 1945 on we think it has no significance whatsoever. But even in the first two years, it is only one factor, and we do not feel it is conclusive, and we think that it is overcome by the strong preponderating evidence that [122] these trusts were created, and the trusts

purchased an interest in the partnership business for the sole purpose of building up an estate for these children.

Now, they start with a $30,000.00 contribution. They, of course, hope that by the time the children reach maturity to have built that up to a good substantial sum.

The evidence is clear that they searched for possible investments. As we look back on it now, I think, and perhaps your Honor thinks, and Mrs. Smith testified that she thought they may have made a mistake in not picking up some of the real estate they looked at. But it is very simple, when you look back years later, to see how you made a mistake.

We moved out here in 1919, and my heart bleeds when I think of all the property we could have bought for a song, and didn't.

So when you look back, and I gather from the tenor of Mrs. Smith's testimony, she was a little sorry they did not pick up some of the real estate that they did look at.

But they did investigate those possibilities of investment for their children, and after investigating several possibilities, and discussing it with their attorneys, their advisers at the bank, and so on, they concluded, on the advice of all these people, the best thing they could do to build up an estate for their children was to put it in the business that Mr. Smith knew from years of experience, and which was [123] a profitable business, and the indications were that it would continue to build up

a substantial estate for the children. So they finally concluded that that was the best for their children, and they followed that course.

Now, all of the indications are that they did not do this for tax purposes, and, as my associate has pointed out, they provided for their own drawing accounts, they did not give the children one-fourth interest in the partnership, the trusts were created on a completely irrevocable basis, the trust assets were set aside, were handled separately, and were gradually built up in investments in bonds and savings accounts, and we feel that the evidence is very compelling, your Honor, in this case more than any of the others, that this was a legitimate business transaction, not entered into for the purpose of avoiding income taxes.

If I may, despite the—I almost hesitate to do this. Your Honor knows this field so well, but I would like to just cite a few cases, additional cases, that may have escaped your attention.

Your Honor has mentioned several of your own, and one that you haven't mentioned, and I know you have it in mind, is your Osbrink case, where your Honor did sustain the partnership. And another case by Judge Harrison, very similar to this, Flandrick vs. United States.

The Court: I have forgotten the Osbrink case. What [124] kind of business was it? I have written so many opinions it is hard for me to remember which it is. What was the Osbrink case?

Mr. Lund: That is where the minor's uncle was the trustee.

The Court: Is that the one where the husband and wife were separated, and it involved a daughter and a son? Is that the Osbrink case?

Mr. Lund: In this case the minor's uncle was the trustee. He was the active manager of the partnership in his capacity as trustee, and the partnership was sustained in that case.

I must confess, your Honor, I was afraid you would embarrass me by asking me some questions about these tax cases. I am not a tax lawyer, and I am not familiar with them, but we do have the Osbrink case as one of the partnership cases your Honor recently decided, where the trusteeship relationship with a partnership existed, as here, and, nevertheless, the partnership arrangement was recognized for income tax purposes.

The case of Judge Harrison's, Frandrick vs. United States, 99 Fed. Supp. 718, is very similar.

Then there are two cases, one a Circuit Court decision, and one a District Court decision, where you have a situation almost identical with this, with husband and wife as partners in a dual capacity as trustees for their children and in their [125] separate and individual capacities.

One of them is Miller vs. Commissioner, 203 Fed. (2d) 350. That is the Circuit Court decision. The other is Maurice vs. Scofield, Western District of Texas, 1952, Paragraph 72,248.

And your Honor is probably familiar with the two Tax Court decisions, which we think sustain our position, and which were recently affirmed by the Ninth Circuit Court, Edward D. Sulton, 18 Tax

Court 715, and Thomas H. Broadhead, 18 Tax Court 726.

Your Honor may want to, if you have an opportunity, to look at those cases.

I feel that very strongly, your Honor, the evidence supports the plaintiffs' case, and judgment should be with the plaintiffs.

Thank you very much.

The Court: What was the citation on that Miller case? 203 Fed. (2d)?

Mr. Lund: 203 Fed. (2) 350.

The Court: All right. Anything further, gentlemen?

(No response.)

The Court: The matter will stand submitted.

Mr. Lund: Thank you, your Honor.

The Court: I will get to it as soon as I have a chance to look at these exhibits.

[Endorsed]: Filed November 3, 1954.

PLAINTIFFS' EXHIBIT No. 1

[Title of District Court and Cause No. 15161.]

STIPULATION

It is hereby stipulated by and between the parties hereto through their respective counsel of record as follows:

I.

The only issue for decision by the Court is to what extent, if any, the Trusts for plaintiffs' minor

children are to be recognized as partners for Federal income tax purposes. Counsel agree that, in accordance with the Court's decision on said issue the amount, if any, of the judgment can and will be computed by them pursuant to Local Rule 7(h).

II.

All statutory and procedural steps necessary to be taken by plaintiffs prerequiste to the maintaining of this action by them have been duly taken by said plaintiffs within the time and in the manner required by law. Counsel agree to join in the preparation of findings of fact which will so show.

III.

On December 29, 1943 there was filed in the office of the County Clerk of Los Angeles County, California, and published as required by law, a Fictitious Name Certificate which stated that Jack Smith, Rose Mae Smith, Jack Smith Trustee of the Barbara Ann Smith Trust, and Rose Mae Smith Trustee of the Howard Samuel Smith Trust were and had been since October 1, 1943 conducting a wholesale shoe jobbing business under the fictitious firm name of Boston Shoe Company.

IV.

On February 16, 1945 there was filed and published as above a Fictitious Name Certificate which stated that Jack Smith, Rose Mae Smith, Jack Smith Trustee of the Barbara Ann Smith Trust, Rose Mae Smith Trustee of the Howard Samuel

Smith Trust, and Herman Weiskaupt were and had been since January 1, 1945 conducting a wholesale shoe jobbing business under the fictitious firm name of Boston Shoe Company.

Dated: This 18th day of June, 1954.

LATHAM & WATKINS,
/s/ By HENRY C. DIEHL,
Attorneys for Plaintiffs

LAUGHLIN E. WATERS,
United States Attorney
EDWARD R. McHALE,
Assistant U. S. Attorney, Chief, Tax Division
BRUCE I. HOCHMAN,
Assistant U. S. Attorney
/s/ BRUCE I. HOCHMAN,
Attorneys for Defendants

PLAINTIFFS' EXHIBIT No. 2

AGREEMENT OF PURCHASE BY HUSBAND OF COMMUNITY INTEREST OF WIFE IN SPECIFIC PROPERTY

This Agreement made and entered into this 31st day of December, 1942, by and between Jack Smith, sometimes hereafter referred to as "Party of the First Part" or "Husband" and Rose Mae Smith, sometimes hereinafter referred to as "Party of the Second Part" or "Wife";

Plaintiffs' Exhibit No. 2—(Continued)

Witnesseth:

Whereas, the parties hereto are husband and wife, having been married on or about the 24th day of May, 1931; and

Whereas, Party of the First Part is doing business under the firm name and style of Boston Shoe Company, with his principal place of business at 826 South Los Angeles Street, Los Angeles, California; and

Whereas, of the capital of said business the sum of $205,867.79 is the community property of the parties hereto, having been acquired since the marriage of the parties hereto and other than by gift, devise, bequest or descent and not the issues and profits of the separate property of Party of the First Part; and

Whereas, the Party of the First Part is desirous of purchasing the community interest of Party of the Second Part in and to said business so that the entire of said business from and after the date hereof shall be the sole and separate property of said Party of the First Part, free and clear of all right, title, interest or estate on the part of the said Party of the Second Part by reason of the marital relations heretofore, now and hereafter existing between these parties, and Party of the Second Part being desirous of receiving the reasonable value of her community interest therein, so that said value and the proceeds thereof shall be her sole and separate property, free and clear from all right, title, interest or estate on the part of the Party of the

Plaintiffs' Exhibit No. 2—(Continued)

First Part by reason of the marital relations heretofore, now and hereafter existing between the parties hereto,

Now, Therefore, It Is Hereby Agreed:

1. Party of the First Part does hereby purchase from Party of the Second Part and Party of the Second Part does hereby sell unto said Party of the First Part, all of the community right, title, interest and estate of said Party of the Second Part in and to the said business commonly known and described as "Boston Shoe Company".

2. Party of the First Part does hereby agree to pay unto Party of the Second Part for her said community interest in and to said business, the sum of $102,933.89, said sum being a full one-half of the reasonable value of the entire of the community property interest of the parties hereto therein.

In payment thereof, Party of the First Part shall, concurrently with the execution hereof, deliver unto Party of the Second Part four negotiable promissory notes of the said Party of the First Part, the first in the principal sum of $30,000.00 due on or before one year, the second in the principal sum of $30,000.00 due on or before two years, the third in the principal sum of $30,000.00 due on or before three years and the fourth in the principal sum of $12,933.89, due on or before four years. Each note shall bear interest from the date hereof until paid, at the rate of 10% per annum.

Party of the Second Part does hereby accept said

Plaintiffs' Exhibit No. 2—(Continued)

promissory notes as payment for her said community interest in and to said business.

3. From and after the date hereof, the said business commonly described as "Boston Shoe Company", with its principal place of business as aforesaid at 826 South Los Angeles Street, Los Angeles, California, together with all of its assets shall be the sole and separate property of Party of the First Part, free and clear from any and all right, title, interest or estate on the part of Party of the Second Part by reason of the marital relations heretofore, now and hereafter existing between the parties hereto.

4. From and after the date hereof, the said sum be $102,933.89, together with the profits and issues that shall be earned thereon, represented by said promissory notes executed concurrently herewith by said Party of the First Part unto said Party of the Second Part and said promissory notes, shall be the sole and separate property of Party of the Second Part free and clear from all right, title, interest or estate on the part of Party of the First Part by reason of the marital relations heretofore, now and hereafter existing between the parties hereto.

5. This agreement is without prejudice to the right, title, interest and estate of Party of the Second Part in and to any other community property owned by her and said Party of the First Part, it being the intention hereby to terminate the community interest of said Party of the Second Part only in and to the specific property involved, to-wit,

Plaintiffs' Exhibit No. 2—(Continued)

the said Boston Shoe Company, a fictitious firm composed of Party of the First Part and other therefrom, any other property owned by the parties hereto as the community property of the parties hereto shall, insofar as this agreement is concerned, remain and continue to be the community property of the parties hereto.

6. This agreement is executed in triplicate; each triplicate is hereby declared to be an original; said triplicates, however, shall constitute but one and the same agreement.

7. This agreement shall inure to the benefit of and be binding upon the heirs, executors, administrators, successors and assigns of the respective parties hereto.

In Witness Whereof, the parties hereto have hereunto set their hands and seals the day and year first hereinabove written.

/s/ By JACK SMITH,
Party of the First Part or Husband.

/s/ By ROSE MAE SMITH,
Party of the Second Part or Wife.

State of California,
County of Los Angeles—ss.

On this 31st day of December, 1942, before me, Gertrude Harris, a Notary Public in and for said County and State personally appeared Jack Smith and Rose Mae Smith, known to me to be the persons whose names are subscribed to the within instru-

Plaintiffs' Exhibit No. 2—(Continued)

ment, and acknowledge to me that they executed the same.

In Witness Whereof, I have hereunto set my hand and affixed my official seal the day and year in this certificate first above written.

[Seal] GERTRUDE HARRIS,
Notary Public in and for said
County and State.

PLAINTIFFS' EXHIBIT No. 3

$30,000.00 December 31st, 1942

On or before 1 year after date, without grace I promise to pay to the order of Rose Mae Smith Thirty Thousand and No/100 Dollars, For Value received, with interest from date at the rate of Ten per cent per annum until paid. Principal and interest payable in Lawful Money of the United States at Los Angeles, California, and in case suit is instituted to collect this note or any portion thereof, I promise to pay such additional sum as the Court may adjudge reasonable as Attorney's fees in said suit.

/s/ Jack Smith

Due 12/31/43

Pay to the Order of Jack Smith. Signed Rose Mae Smith.

PLAINTIFFS' EXHIBIT No. 4

$30,000.00 December 31st, 1942

On or before 2 years after date, without grace I promise to pay to the order of Rose Mae Smith Thirty Thousand and No/100 Dollars, For Value received, with interest from date at the rate of Ten per cent per annum until paid. Principal and interest payable in Lawful Money of the United States at Los Angeles, California, and in case suit is instituted to collect this note or any portion thereof, I promise to pay such additional sum as the Court may adjudge reasonable as Attorney's fees in said suit.

Due 12/31/44. /s/ Jack Smith

Pay to the Order of Jack Smith. Signed Rose Mae Smith.

PLAINTIFFS' EXHIBIT No. 5

$30,000.00 December 31st, 1942

On or before 3 years after date, without grace I promise to pay to the order of Rose Mae Smith Thirty Thousand and No/100 Dollars, For Value received, with interest from date at the rate of Ten per cent per annum until paid. Principal and interest payable in Lawful Money of the United States at Los Angeles, California, and in case suit is instituted to collect this note or any portion thereof, I promise to pay such additional sum as the Court may adjudge reasonable as Attorney's fees in said suit.

Due 12/31/45. /s/ Jack Smith

Pay to the Order of Jack Smith as Original Trustee of the Barbara Ann Smith Trust, a Voluntary Express Trust. Signed Rose Mae Smith.

Pay to the order of Jack Smith, individually, in pursuance to agreement of sale and purchase of undivided interest in property.

PLAINTIFFS' EXHIBIT No. 6

$12,933.89 December 31st, 1942

On or before 4 years after date, without grace I promise to pay to the order of Rose Mae Smith Twelve Thousand Nine Hundred Thirty-Three and 89/100 Dollars, For Value received, with interest from date at the rate of Ten per cent per annum until paid. Principal and interest payable in Lawful Money of the United States at Los Angeles, California, and in case suit is instituted to collect this note or any portion thereof, I promise to pay such additional sum as the Court may adjudge reasonable as Attorney's fees in said suit.

Due 12/31/46. /s/ Jack Smith

PLAINTIFFS' EXHIBIT No. 7

DECLARATION OF TRUST

Know All Men by These Presents:

That Jack Smith, hereinafter sometimes designated as "Original Trustee", hereby declares that Rose Mae Smith, hereinafter sometimes designated as "Trustor", has conveyed, transferred, assigned and set over unto the "Original Trustee", without consideration, that certain promissory note dated

Plaintiffs' Exhibit No. 7—(Continued)

the 31st day of December, 1942, in the principal sum of Thirty Thousand Dollars ($30,000.00), to-(10%) per annum, executed by Jack Smith, the "Original Trustee".

Said property, and the right, title, interest and estate therein, so conveyed and transferred to the "Original Trustee" and all other property and proceeds at any time subject to this trust, shall constitute and be designated as the "Trust Estate".

The Trustor, Rose Mae Smith, does hereby declare that the property conveyed by her unto the Original Trustee hereunder is her sole and separate property, and that Jack Smith has no right, title, interest or estate therein by reason of the marital relations existing between himself and herself. Jack Smith, by accepting this Trust, and agreeing to act as the Original Trustee hereunder, agrees that said property is the sole and separate property of the said Rose Mae Smith, and that he, the said Jack Smith, has no right, title, interest or estate therein by reason of the marital relations heretofore and now existing between himself and his said wife, Rose Mae Smith.

The Trustee has received and shall hold the Trust Estate upon the trusts, with the powers and subject to the limitations as follows, to-wit:

Article I.

(1) In the event of and upon the death, incapacity, removal, resignation or refusal to act on the part of the Original Trustee during the term, exist-

Plaintiffs' Exhibit No. 7—(Continued)

ence and duration of this Trust and prior to the complete distribution of the Trust Estate, then and in that event, Ben Breiman Smith and Ben W. Finkel shall be and are hereby designated and appointed as the Successor Trustees, in the place and stead of such Trustee. In the event that the said Ben Breiman Smith and Ben W. Finkel shall not be alive at said time, or in the event that both of the said Trustees shall die or become incapacitated or be removed or refuse to act, then and in any of said events, the Union Bank & Trust Co. of Los Angeles, shall be and is hereby designated and appointed as a Successor Trustee, in the place and stead of such Trustees.

The Successor Trustee hereby appointed shall, upon the acceptance of this Trust as hereinafter provided, become vested with all of the rights, powers, duties and liabilities herein conferred and imposed upon the Trustee.

(2) Each Successor Trustee, upon the occurrence of the event upon which he or it is to administer this Trust, shall execute, acknowledge and deliver to the then living beneficiaries hereunder a written acceptance of such appointment and thereupon such Successor Trustee, without further action, shall become fully vested with all of the duties, estates, rights, powers and authority of a Trustee hereunder.

In the event that the said Ben Breiman Smith and Ben W. Finkel, though alive, shall both fail to so execute and deliver such written acceptance

Plaintiffs' Exhibit No. 7—(Continued)

within thirty (30) days of the occurrence of the event upon which they are to administer this Trust as the Trustees hereof, then and in that event, the said Union Bank & Trust Co. of Los Angeles, as the next in order of said Successor Trustee shall, within thirty (30) days thereafter (that is, after the expiration of the thirty (30) day period within which the said Ben Breiman Smith and Ben W. Finkel should have given notice of acceptance) make and deliver its instrument of acceptance and thereupon shall act as the Trustees hereunder.

(3) Throughout this Trust, the word "Trustee", when no words of description appear, as "Original Trustee" or "Successor Trustee", shall refer to and mean whomsoever shall be acting as Trustee hereunder.

(4) Jack Smith, Ben Breiman Smith, Ben W. Finkel and the Union Bank & Trust Co. of Los Angeles shall not be required to give any bond or security for the performance of his or its duties hereunder.

In the event, however, that any other person, firm or entity becomes a Trustee hereunder, such Trustee shall give a bond, executed by a good and sufficient corporate surety, conditioned for the faithful performance of the duties of such Trustee hereunder, and for the true and faithful accounting and payment to the beneficiaries hereunder as by this Trust provided, of the Trust Estate; said bond shall be in an amount equal to one-half of the then fair market value of the Trust Estate hereunder;

Plaintiffs' Exhibit No. 7—(Continued)

the premium or cost of said bond shall be a cost of administration hereunder.

Article II.

(1) Neither Jack Smith, Ben Breiman Smith nor Ben W. Finkel, while acting as Trustees hereunder, shall be entitled to any compensation for his services hereunder as such Trustee.

(2) The Union Bank & Trust Co. of Los Angeles and/or any other national banking association qualified to transact business within the State of California who shall become a Trustee hereunder, while acting as Trustee hereunder, shall be entitled to reasonable compensation, not exceeding the following, to-wit:

(a) For the acceptance and undertaking hereof one-tenth of one per cent (1/10th of 1%) of the reasonable value of the corpus of the trust estate, with a minimum fee of Twenty-five Dollars ($25.00); and a like percentage for its acceptance of any property thereafter added thereto;

(b) For its ordinary and usual duties as Trustees hereunder, an annual compensation, payable quarterly, of six tenths of one per cent (6/10ths of 1%) of the reasonable value of such part of the trust estate as shall consist of personal property, and three-fourths of one per cent (¾ of 1%) per annum, payable quarterly, of the reasonable value of the remainder of the trust estate, with a minimum fee of Fifty Dollars ($50.00) per annum.

(c) On any revocation hereof, in whole or in part, or on any withdrawal of the whole or any part

Plaintiffs' Exhibit No. 7—(Continued)

of the trust estate, one-tenth of one per cent (1/10th of 1%) of the reasonable value of the trust estate withdrawn, with- (sic) drawn, with a minimum fee of twenty-five dollars ($25.00); on every other termination of this trust and on every distribution of principal hereunder one per cent (1%) of the reasonable value of the trust estate distributed.

(d) For any unusual or extraordinary services rendered by it as Trustee, including litigation, a reasonable additional compensation.

Article III.

The Trustees shall receive and collect the corpus and income of said Estate and hold, apply, use and distribute the same in the order and priority as follows, to-wit:

(a) To the payment of any and all income taxes and other taxes, general and special assessments, and all costs, charges, attorneys' fees, accountants' fees, expenses and liabilities, including compensation under the provisions of division (2) of the foregoing Article II of the Trustees, expended or incurred or suffered in the collection, care, holding, administration, protection or distribution of the Trust Estate, for the payment of which the Trust Estate and/or the Trustees may become chargeable, including the protection of this Trust and the defense hereof against legal attack.

(b) Only in the event that Barbara Ann Smith (sometimes hereinafter designated as "Primary Beneficiary") shall die after attaining her major-

Plaintiffs' Exhibit No. 7—(Continued)

ity, the Trustee may, in his discretion and without being in any event required so to do, and before the Trust Estate is wholly distributed;

(1) Expend any part of the whole of the Trust Estate towards the payment of the whole or any part of the last illness and burial expenses of the said Barbara Ann Smith; and/or

(2) Expend any part or the whole of the Trust Estate toward the payment of any part or the whole of any assessment of property, income, estate and/or inheritance taxes which may then be levied and unpaid against the said Barbara Ann Smith or her estate.

(c) Income:

(1) During the minority of Barbara Ann Smith, the Primary Beneficiary and, in the event of her death during the minority of Howard Samuel Smith, and unless distribution of the Trust Estate be made prior thereto as hereinafter provided, the income hereof shall be by the Trustee accumulated and become a part of and distributed as a part of the corpus thereof.

(2) No accumulation of income shall be permitted by any provision of this Declaration of Trust at any time, or to any extent, in contravention of law.

(d) Corpus:

The Trustee hereunder shall in all events distribute the Trust Estate to the following persons, in the following proportions and amounts, and in the following order, priority and times, to-wit:

(1) The entire thereof unto Barbara Ann Smith,

Plaintiffs' Exhibit No. 7—(Continued)

at the following times and in the following installments, to-wit:

a. One-fourth (¼) thereof upon the said Barbara Ann Smith attaining the age of twenty-five (25) years.

b. One-fourth (¼) thereof upon the said Barbara Ann Smith attaining the age of thirty (30) years.

c. The balance upon the said Barbara Ann Smith attaining the age of thirty-five (35) years.

d. The Trustee may, in his absolute, arbitrary and uncontrolled discretion, commencing with the attaining by said Primary Beneficiary of her twenty-first year, advance and pay unto said Primary Beneficiary from, but not in excess of, the next succeeding installment to which said Primary Beneficiary might thereafter be entitled, such sums and at such times as to said Trustee, in his absolute, arbitrary and uncontrolled discretion, shall appear proper, necessary or essential for the maintenance, support, medical attention, care and happiness of said Primary Beneficiary, excepting only that during the period from said Primary Beneficiary attaining his majority and until she shall attain the age of twenty-five (25) years, the Trustee shall not advance unto her in excess of the sum of Five Thousand Dollars ($5,000.00) in any one year or ten per cent (10%) of the Trust Estate in any one year, whichever is the smaller, nor during said period in excess of the installment to which said Primary Beneficiary shall be entitled upon attaining the age of twenty-five (25) years; and during the period

Plaintiffs' Exhibit No. 7—(Continued)

from said Primary Beneficiary's twenty-fifth year until she shall have attained the age of thirty (30) years, not to exceed Ten Thousand Dollars ($10,000.00) in any one year nor twenty per cent (20%) of the Trust Estate during any one of said years, whichever is the smaller; and not exceeding the share which said Primary Beneficiary shall be entitled to receive at the age of thirty (30) years; and during the period from said Primary Beneficiary's thirtieth year until she shall attain the age of thirty-five (35) years, not to exceed Fifteen Thousand Dollars ($15,000.00) in any one year nor twenty per cent (20%) of the Trust Estate in any one year, whichever is the smaller.

e. In the event that said Primary Beneficiary shall die prior to the distribution to her of the entire of said Trust Estate, then and in that event the undistributed portion thereof to which said Primary Beneficiary would otherwise be entitled, shall be distributed unto the following persons and in the following order and priority, to-wit:

Firstly: In the event that said Primary Beneficiary shall leave legitimate issue surviving her, then and in that event the Trustee shall distribute unto said issue per stirpes and not per capita, in one lump sum, the remainder of the Trust Estate.

In the event, however, that the said Primary Beneficiary shall not leave surviving her any such legitimate issue, then and in that event the said provision in trust made for said issue shall lapse.

Secondly: In the event that Howard Samuel

Plaintiffs' Exhibit No. 7—(Continued)

Smith, brother of the Primary Beneficiary, be alive, then and in that event the remainder of the Trust Estate shall be distributed in one lump sum unto the then Trustees of the Howard Samuel Smith Trust, a Voluntary Express Trust, created by Jack Smith, his father, and be distributed as by the provisions thereof provided.

In the event, however, that the said Howard Samuel Smith shall not have survived the said Barbara Ann Smith, then and in that event the provision in trust made for him hereby shall lapse.

Thirdly: In the event that the said Howard Samuel Smith shall have left surviving him and alive at the time of the death of the said Barbara Ann Smith, legitimate issue, then and in that event the said remainder of the Trust Estate shall be distributed in one lump sum unto said issue per stirpes and not per capita.

In the event, however, that the said Howard Samuel Smith shall not have left surviving him and alive at said time, any such issue, then and in that event the provision in trust made for such issue hereby shall lapse.

Fourthly: In the event that the provisions in trust under the foregoing sub-paragraphs shall lapse, but if Jack Smith, father of the said Barbara Ann Smith and Howard Samuel Smith, shall be alive, then and in that event, the entire of said undistributed portion of said Trust Estate shall be distributed in one lump sum unto the said Jack Smith.

Plaintiffs' Exhibit No. 7—(Continued)

In the event, however, that the said Jack Smith shall not have survived the said Barbara Ann Smith and the said Howard Samuel Smith, then and in that event, the provision in trust made hereby for him shall lapse.

Fifthly: In the event that the provisions in trust under the foregoing sub-paragraphs Firstly, Secondly, Thirdly and Fourthly shall lapse, then and in that event the entire of said undistributed portion of said Trust Estate shall be distributed unto the then living heirs at law, under the laws of succession of the State of California, of the last to die of the said Barbara Ann Smith, the said Howard Samuel Smith and the said Jack Smith, excluding, however, the Trustor, Rose Mae Smith.

Article IV.

Any income or corpus payable by the Trustee under any provision of this instrument, shall not be pledged, assigned, transferred, sold, or in any manner whatsoever accelerated, anticipated, mortgaged, encumbered or hypothecated by the beneficiaries, nor shall any income or corpus be in any manner subject or liable in the hands of the Trustees for the debts, contracts, obligations, liabilities or engagements of any beneficiary, or be subject to any assignment, voluntary or involuntary, or any other voluntary or involuntary alienation or disposition whatsoever.

Should any beneficiary attempt in any manner to anticipate, dispose of, encumber or charge his or

Plaintiffs' Exhibit No. 7—(Continued)

her interests, whether income or corpus, or any part thereof, or in the event of the bankruptcy or the rendition of any judgment or decree against the interests, whether income or corpus, of such beneficiary, or the levy of any execution or writ of attachment or garnishment thereon, then such income or corpus which would otherwise be paid over directly to such beneficiary, in the discretion of the Trustees, shall be applied directly for his or her support or maintenance, or the support or maintenance of his or her family (excluding any separated or divorced sponse), or both, or be allowed, in the sole discretion of the Trustees, to accumulate in the hands of the Trustee, to be invested and controlled and to be distributed to the next beneficiary in order hereunder; provided, however, that any such accumulations or any part thereof, may be applied from time to time by the Trustees, as the Trustees may deem proper or desirable, in like manner as if the same were a part of the current income derived from the trust fund. It is the intention hereof, among other things, that the interests, whether income or corpus, of the beneficiaries, shall not under any circumstances be liable to or available for the payment of allowance of alimony or settlement in favor of a separated or divorced spouse.

If any provision of this Article shall be deemed illegal, unlawful or void, the same shall not in any wise affect or impair any other provision of this Article or any other provision of this Declaration of Trust.

Plaintiffs' Exhibit No. 7—(Continued)

Article V.

(1) To carry out the provisions of this Trust, and in aid of and incidental to its execution, its management and administration, the Trustee shall be and is vested with the following additional powers and discretions:

(a) Under no circumstances may the Trust Estate or any part or portion thereof be used for the performance, directly or indirectly, of any legal obligation on the part of the Trustor.

(b) The powers, right and discretions hereinafter in this Article V provided, are upon the express limitation hereinbefore in subdivision (a) of this division (1) of this Article V provided.

(c) The Trustees are vested with title to the trust estate as the absolute owners thereof. As such owners, said Trustees may invest said Trust Estate in any property, whether real, personal or mixed and whether legal for investment of trust funds or not and said Trustees shall not be restricted in investments of the Trust Estate to investments legal for trust funds. Said Trustees may by way of specification and not by way of limitation invest the trust estate or any part thereof in any business or may become a partner in any business or stockholder of any corporation or a member of any other form of business entity. In the event that said Trustees shall become a partner in any business, said Trustee shall have the right and power to join with the remaining partners of said business in conveying the entire thereof unto a corporation to

Plaintiffs' Exhibit No. 7—(Continued)

be formed under the laws of the State of California and to receive in exchange for such partnership interest, a like proportionate interest in the stock that shall be issued by such corporation for the entire of the partnership assets, including the interest of the Trustees.

(d) The Trustees are hereby expressly authorized to take, hold, operate and continue to hold and operate, as a part of the Trust Estate hereunder, and without liability for depreciation, loss, or otherwise, any and all property, including any business belonging to the Trust Estate, although not of a character authorized by trust investments.

(e) The Trustees hereunder are hereby authorized to incur and pay for any services, whether legal, accounting or otherwise, deemed necessary in the performance of this Trust, and such expense shall be payable in the order and priority as hereinafter provided.

(f) Said Trustees are hereby expressly authorized and invested with power to hold all shares of stock and other securities belonging to this Trust at any time in the name of any nominee; to vote any shares of stock in person or by proxy; to assert or waive any stockholder's right or privilege in respect thereto, including any right or privilege to subscribe for or otherwise acquire any additional stock; to assent to any merger, consolidation or reorganization of any property, corporation, or enterprise in which the Trustees may be interested, by virtue of this Trust, or whose obligations or se-

Plaintiffs' Exhibit No. 7—(Continued)

curities may be held hereunder, for such other securities as may be issued pursuant to such action or arrangement; to unite with other owners of similar properties or securities in any plan, agreement, deposit or trust designed to effectuate any such purpose, and to pay all assessments or expenses incidental thereto; to assent to any lease, or other corporate act.

(g) To join or unite with any other stockholder, or stockholders, or any party beneficially or otherwise interested in any shares of stock of any corporation in which this Trust may be a stockholder, for the purpose of securing the more efficient management of such corporation, and to that end may also enter into any voting trust or lawful agreement to concentrate or unify the control of any stock of any such corporation embodying such terms and provisions as may appear acceptable to the Trustees, and to deposit the shares or interest held by them hereunder under any trust or agreement, all as the Trustees may in their own judgment deem prudent.

(h) To reimburse themselves from the income and/or the corpus of the Trust Estate, for any loss, liability or expenses incurred by reason of the ownership or holding of any property received or held in this Trust and/or by reason of their use or operation of any thereof, unless caused by the Trustees' personal (not imputed) gross negligence.

(i) To borrow money and, in such manner and in accordance with such procedure, and through such

Plaintiffs' Exhibit No. 7—(Continued)

means or agency as said Trustees may deem advisable; to mortgage, pledge, transfer in trust, or otherwise encumber and/or render liable the whole or any part of the Trust Estate for the repayment of any monies so borrowed and/or as security therefor.

(j) To determine, in their discretion, what is principal of the Trust Estate, gross income or net distributable income therefrom, except that all bonuses, royalties and recoveries from mines, gas or oil leases or wells, all stock dividends and proceeds of sale of stock rights and all cash dividends (other than liquidating dividends stated in writing to be such by the corporation paying the same or proved to the satisfaction of the Trustees to be such prior to their disbursement thereof,) shall go to income, and all gain or loss which shall result from payment, retirement or sale of stocks, notes, bonds or other securities or on foreclosure or other realization upon mortgages and trust deeds, shall inure to and fall upon principal of the Trust Estate. The net income from real property acquired by the Trustees on, or by acceptance of conveyance in lieu of, foreclosure shall go to income of the Trust Estate. Brokers' or other commissions and expenses on purchase or sale of trust property shall be charged against principal. The Trustees are directed to charge all premiums on investments against principal, and to credit all discounts on investments to principal. The Trustees shall not amortize from income premiums paid from principal.

Plaintiffs' Exhibit No. 7—(Continued)

(k) To hold property of the Trust Estate in their own name or in the name of their nominee or nominees, with or without disclosure of fiduciary relationship, the Trustees being responsible for the acts of any such nominee affecting such property.

(l) To manage, control, sell, convey, exchange, partition, divide, subdivide, improve or repair any or all property of the Trust Estate; in connection with any disposal of property, to grant options and to sell upon deferred payments.

(m) The Trustees may maintain and administer the Trust Estate undivided and as a unit and shall not be required to make physical division or segregation thereof except if, when and to the extent required to make distribution therefrom as in this Trust provided, and the Trustees, in performing and fulfilling any of the provisions hereof, may pay any sum or make any distribution in kind.

(n) To allot, partition and distribute the Trust Estate at such valuations and according to such method of procedure as the Trustees may determine upon whenever such act shall be required or advisable, and to do so in kind or partly in kind and partly in money, according to its valuation thereof; upon termination of this Trust and in aid of and incidental to distribution hereunder, forthwith to sell such property as in the Trustees' discretion may be necessary in order to make or equalize distributions.

(o) Nothing herein contained shall be deemed to compel the Trustees to sell any of the assets or

Plaintiffs' Exhibit No. 7—(Continued)

properties of the Trust received at the time of the creation hereof or hereafter from the Trustor, nor prevent or restrict the Trustees from investing any or all of the Trust Estate in any business, nor from becoming a partner in any business or stockholder of any corporation or member of any other form of business entity in which Trustor is interested, as a partner, stockholder or otherwise.

(p) The Trustees may construe this Trust, and any provision thereof, and may act upon such construction without liability, except for bad faith in construing this Trust, or any provision hereof, or her wilful misconduct.

(q) The Trustees may pay out of principal or income, as they may elect, or partially out of each in such shares as they may determine, property and other taxes, assessments, charges, expenses and attorneys' fees incurred in the administration or protection of this Trust, and the Trustees' compensation as herein fixed. The discretion of the Trustees to pay said items from income or principal may be exercised not only in the interest of the Trust Estate, but for the benefit of any beneficiary.

(r) All discretions conferred upon the Trustees by this instrument shall, unless specifically limited, be absolute and uncontrolled, and their exercise conclusive on all persons interested in this Trust or the Trust Estate. The enumeration hereof of certain powers of the Trustees is not intended to limit their general powers.

(2) Income accrued or undistributed at the term-

Plaintiffs' Exhibit No. 7—(Continued)

ination of any interest or estate hereunder shall belong and go to the beneficiary or beneficiaries entitled to the next eventual interest in the proportions in which they take such interest.

(3) Unless the Trustees shall receive from some person interested in this Trust, satisfactory written proof of any death, birth, marriage or other event upon which the right to income or principal of the Trust Estate may depend, the Trustees shall not be liable to any person for disbursements made in good faith to persons whose interests shall have been affected by such event.

Article VI.

The Trustee shall under no circumstances be liable in his individual capacity upon or by reason of contracts entered into, or other obligations, whether express, implied, or imposed by law, assumed or undertaken in executing her powers, of performing his duties hereunder, but the rights thereunder of parties to such contracts, or other obligations shall be limited to such, if any, as they may have against such Trustee in his capacity as such.

Article VII.

In all matters, if there be two Trustees acting hereunder, the Trustees shall consult with each other and no Trustee or Trustees shall incur any obligation binding upon this Trust, or dispose of or hypothecate any property of this Trust, or purchase any property for this Trust without notice

Plaintiffs' Exhibit No. 7—(Continued)

to the remaining Trustee or Trustees of their intention so to do. No single Trustee, unless there be but one Trustee acting hereunder, shall have or has any authority to make any representations whatsoever binding upon this Trust, or to dispose of or hypothecate any property of this Trust, or purchase any property for this Trust, if there be more than one Trustee acting hereunder.

Article VIII.

The whole title, legal and equitable, to the Trust Estate is vested in the Trustees, as such title is necessary for the due execution of the Trust. The beneficiaries shall take no interest or estate therein, the interest of the beneficiaries hereunder being personal property only, consisting of the right to enforce the due performance of this Trust.

Article IX.

The duration of this Trust shall in no event, nor by any possibility, extend beyond, but shall wholly cease, at the death of the last survivor of the following persons now in being, to-wit: Jack Smith, Rose Mae Smith, Howard Samuel Smith and Barbara Ann Smith.

Article X.

(1) The Trustor, Rose Mae Smith, declares that she has been fully advised by Alfred Gitelson, an attorney at law, as to the legal effect of the execution of this Declaration of Trust, in so far as the transfer and assignment by her unto the Original Trustee of said Trust Estate is concerned; that she

Plaintiffs' Exhibit No. 7—(Continued)

is aware of the amount of property hereunto transferred and conveyed by her; that she has given due consideration to the question whether the trust created by this Declaration of Trust, in so far as said property transferred by her is concerned, shall be revocable or irrevocable, and she does now declare that this Trust shall be irrevocable.

Article XI.

The Trustor, with the written consent of the Trustees, but not otherwise, may add to the Trust other property which, upon the acceptance thereof by the Trustees, shall become a part of the Trust Estate to be held in trust under all of the terms hereof.

Article XII.

Throughout this Trust, the singular shall include the plural; the masculine shall include the feminine and neuter gender; the word "Trustee" shall include a corporation, as well as a natural person; the word "month" means a calendar month; the word "incapacity", as used with reference to any trustee, shall be construed to mean any person, whether insane or not, who, by reason of old age, disease, weakness of mind, or other cause, is unable, unassisted, properly to manage and take care of the Trust Estate and by reason thereof is likely to be deceived or imposed upon by artful or designing persons; the phrase "legitimate issue" shall be deemed to include any child adopted through a court proceeding for adoption, as is provided by the provisions of Section 221 to 229, inclusive (ex-

Plaintiffs' Exhibit No. 7—(Continued)

pressly excluding Section 230) of the Civil Code of the State of California.

Article XIII.

In the event that any part or portion, paragraph, clause or sentence of this Declaration of Trust shall be hereafter, by a Court of competent jurisdiction, and by a final judgment thereof, declared to be invalid, unlawful, void or unenforcible, such declaration and such invalidity or unenforcibility shall not affect the remaining part of this Trust, it being hereby declared that this Trust would have been entered into and the Trustor would have entered into the remaining portions of this Trust, notwithstanding such unvalidity or unenforcibility, and this Trust shall continue to be effective and binding during the remaining period of the term hereof, notwithstanding the invalidity or unenforcibility of any such part, portion, paragraph, clause, phrase or sentence thereof.

Article XIV.

This Declaration of Trust shall inure to the benefit of and be binding upon the heirs, executors, administrators, successors and assigns of the parties hereto.

This Declaration of Trust is executed in triplicate and each triplicate hereby is declared to be an original; the triplicate together, however, shall constitute but one and the same Trust.

In Witness Whereof, the Original Trustee and

Plaintiffs' Exhibit No. 7—(Continued)

the Trustor have hereunto set their hands and seals this 29th day of September, 1943.

/s/ By JACK SMITH,
Original Trustee.
/s/ By ROSE MAE SMITH,
Trustor.

PLAINTIFFS' EXHIBIT No. 8

DECLARATION OF TRUST

Know All Men By These Presents:

That Rose Mae Smith, hereinafter sometimes designated as "Original Trustee", hereby declares that Jack Smith, hereinafter sometimes designated as "Trustor", has conveyed, transferred, assigned and set over unto the "Original Trustee", without consideration, those certain United States Certificates of Indebtedness, Series B 1944, each dated April 15, 1943, serial numbered 70564, 70565 and 70566, and each in the principal sum of Ten Thousand Dollars ($10,000.00).

[Exhibit 8 is identical with Exhibit 7 except that where the name Rose Mae Smith appears in Exhibit No. 7, Jack Smith appears in Exhibit No. 8, and where the name Jack Smith appears in Exhibit No. 7 Rose Mae Smith appears in Exhibit No. 8. Where the name Barbara Ann Smith appears in Exhibit No. 7 the name Howard Samuel Smith appears in Exhibit

No. 8 and where the name Howard Samuel Smith appears in Exhibit No. 7 the name Barbara Ann Smith appears in Exhibit No. 8.]

PLAINTIFFS' EXHIBIT No. 9

ASSIGNMENT AND TRANSFER BY TRUSTOR TO TRUSTEE UNDER VOLUNTARY EXPRESS TRUST

Know All Men By These Presents:

Whereas, I, the undersigned, Jack Smith, have this date caused to be executed a "Declaration of Trust", whereof Rose Mae Smith is the Original Trustee and Howard Samuel Smith is the Primary Beneficiary and being desirous of making a gift unto said trust,

Now, Therefore, I, Jack Smith do hereby give, assign, transfer and set over unto Rose Mae Smith as Original Trustee of the Howard Samuel Smith Trust, those certain bonds, Series B, of the Government of the United States, which said bonds and the serial numbers are each more particularly described as follows, to-wit:

United States Certificate of Indebtedness, Series B

1944—Issued April 15th, 1943.

Serial Nos. 70564, 70565 and 70566, each in the principal sum of $10,000.00.

Dated this 29th day of September, 1943.

/s/ By Jack Smith, Trustor

Receipt is hereby acknowledged of the bonds above described.

Dated this 29th day of September, 1943.

Rose Mae Smith as original Trustee
of the Howard Samuel Smith
Trust, a Voluntary Express Trust
By Rose Mae Smith

PLAINTIFFS' EXHIBIT No. 10

ASSIGNMENT BY TRUSTOR TO TRUSTEE OF VOLUNTARY EXPRESS TRUST

Know All Men By These Presents:

Whereas, the undersigned, Rose Mae Smith has this date as Trustor, caused a Declaration of Trust to be executed, whereof Jack Smith is Original Trustee, and Barbara Ann Smith is Beneficiary and is desirous of making a gift unto said trust,

Now, Therefore, I Rose Mae Smith, do hereby give, assign, transfer and set over unto the said Jack Smith as Original Trustee of the Barbara Ann Smith Trust, a Voluntary Express Trust, that certain promissory note dated on or about the 31st day of December, 1942, in the principal sum of Thirty Thousand and No/100 ($30,000.00) Dollars, due on or before three years from the date thereof, bearing interest at the rate of ten (10%) per cent

per annum, pursuant whereof, I have endorsed said note unto said Trustee, on the reverse side thereof;

"Pay to the order of the Original Trustee of the Barbara Ann Smith Trust, a Voluntary Express Trust."

Dated this 28th day of September, 1943.

/s/ By Rose Mae Smith, Trustor

Receipt is hereby acknowledged of the bonds above described.

Dated this 29th day of September, 1943.

Jack Smith as Original Trustee of the Barbara Ann Smith Trust, a Voluntary Express Trust
By Jack Smith

PLAINTIFFS' EXHIBIT No. 11

AGREEMENT OF SALE AND PURCHASE OF INTEREST IN SPECIFIC PROPERTY

This Agreement made and entered into this 29th day of September, 1943, by and between Jack Smith, sometimes hereinafter referred to as "Party of the First Part" or "Seller" and Rose Mae Smith, sometimes hereinafter referred to as "Party of the Second Part" or "Purchaser",

Witnesseth:

Whereas, Party of the First Part is the owner as his sole and separate property of and transacting business under the firm name of "Boston Shoe

Plaintiffs' Exhibit No. 11—(Continued)

Company", with its principal place of business at 826 South Los Angeles Street, Los Angeles, California; and

Whereas, said Party of the First Part is indebted unto said Party of the Second Part upon, among others, two certain promissory notes, each in the principal sum of Thirty Thousand and No/100 ($30,000.00) Dollars, each dated the 31st day of December, 1942, each bearing interest at the rate of ten (10%) per cent per annum, one due on or before one year from the said 31st day of December, 1942 and the other due on or before two years from the said 31st day of December, 1942, which said promissory notes are the sole and separate property of said Party of the Second Part; and

Whereas, the said Party of the Second Part is desirous of purchasing an interest in and to the said business of Party of the First Part; and

Whereas, it is the opinion of Party of the First Part that his net capital in and the reasonable value of said business as of the close of business on the 30th day of September, 1943, will be the sum of Two Hundred Thousand and No/100 ($200,000.00) Dollars and that under any circumstances, the net worth and reasonable value of said business as of the said close of business on the 30th day of September, 1943, shall be adjusted to the sum of Two Hundred Thousand and No/100 ($200,000.00) Dollars, the parties hereto agreeing that there is no goodwill of said business; and

Whereas, Party of the First Part is desirous of

Plaintiffs' Exhibit No. 11—(Continued)

selling unto said Party of the Second Part an undivided interest in and to said business and its assets, including the net capital thereof, as of the close of business on the said 30th day of September, 1943, and the parties hereto agreeing that a thirty (30%) per cent interest therein is of a reasonable value of not to exceed Sixty Thousand ($60,000.00) Dollars,

Now, Therefore, It Is Hereby Agreed:

I.

For and in consideration of the sum of Sixty Thousand ($60,000.00) Dollars in hand paid by Party of the Second Part unto Party of the First Part, receipt of which is hereby acknowledged, said sum being paid by the surrender by Party of the Second Part unto Party of the First Part of those two certain promissory notes hereinabove more particularly described, each executed by Party of the First Part, the accrued interest thereon to be paid in cash by Party of the First Part unto Party of the Second Part, Party of the First Part does hereby grant, bargain and sell unto Party of the Second Part a full thirty (30%) per cent in and to said business commonly known as the "Boston Shoe Company" and in and to its assets of every type, nature, kind and description whatsoever, subject to the liabilities to which said assets are subject, as of the close of business on the 30th day of September, 1943.

Plaintiffs' Exhibit No. 11—(Continued)

II.

Party of the First Part does hereby warrant unto Party of the Second Part that his net capital and the reasonable value of said business as of the close of business on the said 30th day of September, 1943, will be the sum of Two Hundred Thousand and No/100 ($200,000.00) Dollars.

The phrase "net capital" as used throughout this agreement, is hereby defined to mean the reasonable market value of the tangible assets of the said Boston Shoe Company, after deducting all liabilities to which said assets and business are subject, without provision for goodwill, the parties hereto hereby agreeing that the said business, Boston Shoe Company, has no goodwill. In the event that the net capital of said Party of the First Part upon the close of business on the said 30th day of September, 1943, shall be less than the said sum of Two Hundred Thousand and No/100 ($200,000.00) Dollars, Party of the First Part shall contribute unto such business such additional cash or other assets which, when added to the assets of said business, shall create a net capital of Two Hundred Thousand ($200,000.00) Dollars; in the event that the net capital of Party of the First Part, upon the close of business on said September 30th, 1943, shall exceed said sum of Two Hundred Thousand and No/100 ($200,000.00) Dollars, the excess of the said net capital shall be deemed a loan from Party of the First Part unto said business, repayable unto him upon demand, without, however, any interest.

Plaintiffs' Exhibit No. 11—(Continued)

An audit shall be made of the affairs of said business as of the close of business on September 30th, 1943, by Meyer Pritkin & Company, Certified Public Accountants and Accountants for said business. By said audit, the net capital of Party of the First Part shall be determined. Said audit, insofar as it shall determine the net capital of said Party of the First Part on the close of business on said September 30th, 1943, shall be binding and conclusive upon both of the parties hereto.

III.

The interest of Party of the First Part in and to said business, being his sole and separate property, shall continue to be his sole and separate property, free and clear of any and all right, title, interest and estate on the part of Party of the Second Part by reason of the marital relations heretofore, now and hereafter existing between the parties hereto.

IV.

The purchase price paid by Party of the Second Part for said interest in and to said business being her sole and separate property, her interest in and to said business acquired hereby shall continue to be her sole and separate property, free and clear from all right, title, interest and estate on the part of the Party of the First Part by reason of the marital relations heretofore, now and hereafter existing between the parties hereto.

Plaintiffs' Exhibit No. 11—(Continued)

V.

This Agreement is executed in triplicate; each triplicate is hereby declared to be an original; said triplicates, however, shall constitute but one and the same agreement.

This Agreement shall insure to the benefit of and be binding upon the heirs, executors, administrators, successors and assigns of each of the parties hereto.

In Witness Whereof, each of the parties have hereunto set their hands and seals the day and year first hereinabove written.

/s/ By JACK SMITH,
Party of the First Part or Seller

/s/ By ROSE MAE SMITH,
Party of the Second Part or
Purchaser

State of California,
County of Los Angeles—ss.

On this 29th day of September, 1943, before me, Gertrude Harris, a Notary Public in and for said County and State, personally appeared Jack Smith, known to me to be the person whose name is subscribed to the within instrument and acknowledged to me that he executed the same.

In Witness Whereof, I have hereunto set my

Plaintiffs' Exhibit No. 11—(Continued)

hand and affixed my official seal the day and year in this certificate first above written.

[Seal] /s/ GERTRUDE HARRIS,
Notary Public in and for said
County and State

State of California,
County of Los Angeles—ss.

On this 29th day of September, 1943, before me, Gertrude Harris, a Notary Public in and for said County and State, personally appeared Rose Mae Smith, known to me to be the person whose name is subscribed to the within instrument, and acknowledged to me that she executed the same.

In Witness Whereof, I have hereunto set my hand and affixed my official seal the day and year in this certificate first above written.

[Seal] /s/ GERTRUDE HARRIS,
Notary Public in and for said
County and State

PLAINTIFFS' EXHIBIT No. 12

AGREEMENT OF SALE AND PURCHASE OF UNDIVIDED INTEREST IN PROPERTY

This Agreement made and entered into this 30th day of September, 1943, by and between Jack Smith, sometimes hereinafter referred to as "Party

Plaintiffs' Exhibit No. 12—(Continued)

of the First Part" or "Seller" and Rose Mae Smith, sometimes hereinafter referred to as "Party of the Second Part", Rose Mae Smith as Original Trustee of the Howard Samuel Smith Trust, a Voluntary Express Trust, sometimes hereinafter referred to as "Party of the Third Part" or "Purchaser" and Jack Smith as Original Trustee of the Barbara Ann Smith Trust, a Voluntary Express Trust, sometimes hereinafter referred to as "Party of the Fourth Part" or "Purchaser",

Witnesseth:

Whereas, Party of the First Part is the owner of an undivided seventy (70%) and Party of the Second Part is the owner of an undivided thirty (30%) per cent in and to that certain business commonly known and described as "Boston Shoe Company", with its principal place of business at 826 South Los Angeles Street, City and County of Los Angeles, State of California; and

Whereas, Rose Mae Smith is the Original Trustee of the Howard Samuel Smith Trust, a Voluntary Express Trust and Jack Smith is the Original Trustee of the Barbara Ann Smith Trust, a Voluntary Express Trust; and

Whereas, Party of the First Part and Party of the Second Part do hereby represent and warrant unto Party of the Third Part and Party of the Fourth Part that the net capital of said business as of the close of business on September 30th, 1943 and the reasonable value of said business will be the

Plaintiffs' Exhibit No. 12—(Continued)

sum of Two Hundred Thousand ($200,000.00) Dollars; and

Whereas, Party of the First Part is desirous of selling unto Party of the Third Part and unto Party of the Fourth Part each, an undivided fifteen (15%) per cent in and to said business as of the close of business on the 30th day of September, 1943, the purchase price of said interest to be based upon the net capital of said business on said date, all of the parties hereto hereby agreeing that said business has no goodwill and Party of the Second Part being agreeable thereto,

Now, Therefore, It Is Hereby Agreed:

I.

For and in consideration of the sum of Thirty Thousand ($30,000.00) Dollars in hand paid, receipt of which is hereby acknowledged from Party of the Third Part, Party of the First Part does hereby grant, bargain and sell unto the said Party of the Third Part a full undivided fifteen (15%) per cent in and to that certain business commonly described as the "Boston Shoe Company" as of the close of business on the 30th day of September, 1943.

II.

For and in consideration of the sum of Thirty Thousand ($30,000.00) Dollars in hand paid, receipt of which is hereby acknowledged from Party of the Fourth Part, Party of the First Part does hereby grant, bargain and sell unto the said Party of the

Plaintiffs' Exhibit No. 12—(Continued)

Fourth Part a full undivided fifteen (15%) per cent in and to that certain business commonly described as the "Boston Shoe Company" as of the close of business on the 30th day of September, 1943.

III.

The phrase "net capital" as herein used is hereby defined to mean the reasonable market value of all the tangible assets of said business commonly known as the "Boston Shoe Company" after providing for the payment of all liabilities to which said assets and said business are subject, all as of the close of business on the 30th day of September, 1943. An audit shall be made of the said business as of the said close of business on September 30th, 1943, by Meyer Pritkin & Company, Certified Public Accountants and Accountants for said business. By said audit, the net capital of said business shall be determined as at said time. In the event that the net capital of said business as at said time is less than the sum of Two Hundred Thousand ($200,000.00) Dollars, Party of the First Part shall pay into said business such sum as shall be necessary to make the net capital thereof said sum. In the event that the net capital of said business as at said time is in excess of said sum, the excess thereof shall be deemed a loan by Party of the First Part unto said business, to be paid to him upon demand, without interest. Any audit made by the said Meyer Pritkin & Company and the determination thereby of the net capital of said business as at the close of

Plaintiffs' Exhibit No. 12—(Continued)

business at said time, to-wit, the 30th day of September, 1943, shall be conclusive upon all of the parties hereto. In any such audit, no value shall be placed upon the name of said business or the goodwill thereof, the parties hereto agreeing that said business has no goodwill.

IV.

This Agreement is executed in quadruplicate; each quadruplicate is hereby declared to be an original; said quadruplicates, however, shall constitute but one and the same agreement.

This Agreement shall inure to the benefit of and be binding upon the heirs, executors, administrators, successors and assigns of each of the parties hereto.

In Witness Whereof, each of the parties have hereunto set their hands and seals the day and year first hereinabove written.

/s/ By JACK SMITH,
Party of the First Part or Seller

/s/ By ROSE MAE SMITH,
Party of the Second Part

Rose Mae Smith as Original Trustee of the Howard Samuel Smith Trust, a Voluntary Express Trust

/s/ By ROSE MAE SMITH,
Party of the Third Part of Purchaser

Plaintiffs' Exhibit No. 12—(Continued)

Jack Smith as Original Trustee of the Barbara Ann Smith Trust, a Voluntary Express Trust
/s/ By JACK SMITH,
Party of the Fourth Part or Purchaser

State of California,
County of Los Angeles—ss.

On this 30th day of September, 1943, before me, Gertrude Harris, a Notary Public in and for said County and State, personally appeared Jack Smith, Rose Mae Smith, Rose Mae Smith as Original Trustee of the Howard Samuel Smith Trust, a Voluntary Express Trust and Jack Smith as Original Trustee of the Barbara Ann Smith Trust, a Voluntary Express Trust, known to me to be the persons whose names are subscribed to the within instrument and acknowledged to me that they executed the same.

In Witness Whereof, I have hereunto set my hand and affixed my official seal the day and year in this certificate first above written.

[Seal] GERTRUDE HARRIS,
Notary Public in and for said County and State

PLAINTIFFS' EXHIBIT No. 13

ARTICLES OF CO-PARTNERSHIP

These Articles of Co-Partnership, made and entered into as of the 1st day of October, 1943, by and between Jack Smith, sometimes hereinafter referred to as "Party of the First Part" or "First Co-Partner", Rose Mae Smith, sometimes hereinafter referred to as "Party of the Second Part" or "Second Co-Partner", Jack Smith As Original Trustee of the Barbara Ann Smith Trust, a Voluntary Express Trust, in his representative capacity, sometimes hereinafter referred to as "Party of the Third Part" or "Third Co-Partner" and Rose Mae Smith As Original Trustee of the Howard Samuel Smith Trust, a Voluntary Express Trust, in her representative capacity, sometimes hereinafter referred to as "Party of the Fourth Part" or "Fourth Co-Partner";

Witnesseth:

Whereas, Party of the First Part is the owner of an undivided forty (40%) per cent and Party of the Second Part is the owner of an undivided thirty (30%) per cent and Party of the Third Part is the owner of an undivided fifteen (15%) per cent and Party of the Fourth Part is the owner of an undivided fifteen (15%) per cent as tenants in common, of that certain business commonly known and described as "Boston Shoe Company", with its principal place of business at 826 South Los Angeles Street, City and County of Los Angeles, State of California; and

Plaintiffs' Exhibit No. 13—(Continued)

Whereas, by reason of the foregoing, all of the parties hereto are desirous of constituting themselves into a co-partnership, upon the terms, conditions and covenants as herein set forth, supplementing the same as hereinafter in Article XIV provided by certain only of the provisions of the Uniform Partnership Act of the State of California.

Now, Therefore, It Is Hereby Agreed:

Article I.

The parties hereto do hereby agree that they are from this time on, for the term and upon the conditions, covenants and agreements hereof, co-partners.

Article II.

1. Said partnership shall be conducted and carried on under the partnership name and style of "Boston Shoe Company".

2. The principal place of business of this co-partnership shall be at Number 826 South Los Angeles Street, City of Los Angeles, County of Los Angeles, State of California, or at such other place as the partners hereto may from time to time designate in writing.

This partnership may have one or more offices, and in any state or territory of the United States, as may be determined and designated in writing by the partners hereto.

Plaintiffs' Exhibit No. 13—(Continued)

Article III.

1. The business of this co-partnership shall be to buy, sell, manufacture and deal in, and to engage in and conduct and carry on the business of buying, selling, manufacturing and dealing in footwear and any other business related thereto and deemed to be for the best interests of the co-partnership.

2. In general, this co-partnership may carry on any business that may be carried on by, and have and exercise all powers that a natural person may regularly carry on or have under the laws of the State of California.

Article IV.

1. The capital of the co-partnership shall consist of the following, to-wit:

A. Contributed Capital:

Party of the First Part, Party of the Second Part, Party of the Third Part and Party of the Fourth Part do hereby sell, assign, transfer, set over and convey unto this co-partnership, all property of every type, nature, kind and description whatsoever, including leases and leaseholds owned by said parties, in undivided interests as tenants in common, in that certain business commonly known and described as the "Boston Shoe Company", situate at 826 South Los Angeles Street, City and County of Los Angeles, State of California, subject to the liabilities to which said assets are subject, all as shall be shown upon a "Statement of Assets and Liabilities of Boston Shoe Company as at the close of business on September 30th,

Plaintiffs' Exhibit No. 13—(Continued)

1943", prepared by Meyer Pritkin & Company, Certified Public Accountants and Accountants for said business. The net capital of said business as of the close of business on September 30th, 1943, is hereby agreed to be the sum of Two Hundred Thousand ($200,000.00) Dollars, by reason whereof, the interest of each of the parties therein is valued at and the contribution of each of the parties to the "Contributed Capital" of this co-partnership is agreed, therefore, to be as follows, to-wit:

Jack Smith: $80,000.00.

Rose Mae Smith: $60,000.00.

Jack Smith, Original Trustee of the Barbara Ann Smith Trust, a Voluntary Express Trust: $30,000.00.

Rose Mae Smith, Original Trustee of the Howard Samuel Smith Trust, a Voluntary Express Trust: $30,000.00.

The phrase "net capital" as herein used, is hereby defined to mean the residue of the reasonable market value of the tangible assets of the said Boston Shoe Company, after deducting and making provision for the payment of all liabilities of said business, existing as of the close of business on the said 30th day of September, 1943, without, however, any provision for goodwill, the parties hereto hereby agreeing that said business has no goodwill.

B. Earned Capital:

Upon the close of the first fiscal year, or calendar year, whichever may be used by this co-partnership for its purposes, and thereafter every year, an

Plaintiffs' Exhibit No. 13—(Continued)

audit shall be made of the business of the co-partnership, and all net profits of the co-partnership earned and collected shall be thereby determined. No provision shall be made in any audit of the affairs of the co-partnership for any value of the goodwill, if any, of the co-partnership. In the event that such audit shall show a net profit earned and collected for such "accounting period", and before any distribution of net profits shall be made to any partner, there shall be first set aside to an "Earned Capital Account" such percentage of the said net profits as the partners shall from time to time determine. Said "Earned Capital Account" so created shall be used as capital of the co-partnership in the operation of the co-partnership business. The net profits remaining after setting aside said per cent to said "Earned Capital Account" are sometimes hereinafter referred to as "distributable net profits".

The said period of each audit is sometimes herein in these Articles of Co-Partnership referred to as "accounting period".

Each partner shall have an interest in the "Earned Capital Account" created by the foregoing provision in the same proportion to which each partner shall share in the losses of the co-partnership, as provided by Article VI hereof.

C. Further Capital:

If at any time or times hereafter further capital be required for carrying on the business and the partners shall determine to increase the capital, the additional capital shall be advanced by the partners

Plaintiffs' Exhibit No. 13—(Continued)

in the same proportion as they are entitled to share in the "distributable net profits".

Article V.

1. The net profits of the co-partnership shall be distributed as follows, to-wit:

A. There shall be first set aside to the "Earned Capital Account" such percentage of the net profits as is provided for by Subdivision B.—"Earned Capital"—of Article IV hereof.

B. To Jack Smith, 40% of the "distributable net profits".

C. To Rose Mae Smith, 30% of the "distributable net profits".

D. To Jack Smith As Original Trustee of the Barbara Ann Smith Trust, a Voluntary Express Trust, in his representative capacity, 15% of the "distributable net profits".

E. To Rose Mae Smith As Original Trustee of the Howard Samuel Smith Trust, a Voluntary Express Trust, in her representative capacity, 15% of the "distributable net profits".

2. There shall be paid to each of the partners hereto who shall render services unto the business of the co-partnership, a salary of such amount and payable at such times as shall be determined by the partners hereto.

Any salary received by any partner under any provision of these "Articles of Co-Partnership" shall be deemed and charged as a part of the cost of doing business of this co-partnership, and not

Plaintiffs' Exhibit No. 13—(Continued)

an advance or charge against the share of the "distributable net profits" to which such partner so receiving said salary is otherwise entitled.

3. Each partner shall be entitled to draw out of and from the "distributable net profits" and/or "Contributed Capital" and/or "Earned Capital" of the co-partnership for his own special account, such amount as the co-partners hereto may from time to time designate.

4. If any partner shall leave in the business, after any "accounting period", any share of such partner's "distributable net profits" (other than the percentage to be set aside to the "Earned Capital Account") the same shall be considered a contribution to the "Contributed Capital" of such partner.

5. If any partner shall advance to the co-partnership at its request any sums, the same shall be considered a debt of such co-partner, but no interest shall be payable thereon.

Article VI.

Each of the partners hereto shall share in the losses of the co-partnership in the same proportion that each is entitled to share in the "distributable net profits".

Article VII.

1. Each partner hereto shall devote so much of his time to the business of the co-partnership as the partners shall from time to time designate.

2. Books of account shall be kept and entries made therein of all monies, goods, checks, receipts,

Plaintiffs' Exhibit No. 13—(Continued)

payments, and all transactions of the co-partnership. Said books of account shall be kept where the business of the co-partnership is to be carried on, and shall be at all times open to the examination of the partners, or either or any of them.

3. All monies of the co-partnership shall be deposited in a bank account, and in the name of the co-partnership. All withdrawals therefrom or checks upon or drafts against said account must be signed by and need only be signed by either the Party of the First Part, or the Party of the Second Part.

4. The co-partnership business shall be managed and carried on, and all contracts, deals or transactions given or taken for any matter or thing concerning the co-partnership, shall be made, given or taken and entered into in the name of the co-partnership.

The co-partnership shall not enter into any contracts, deals, transactions, notes, or any other contract whatsoever whereby it shall be obligated to perform any duty or to render any service or to pay any sum whatsoever, or incur any obligation or liability binding upon the said co-partnership unless consented to by the Party of the First Part during his lifetime and while a partner hereof.

5. No partner shall, during the continuance of this co-partnership, carry on or be concerned or interested financially, directly or indirectly, in the same kind of business as that carried on by this co-partnership, nor be engaged in nor undertake, during the existence hereof, any other trade or business.

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6. No partner hereto shall, without the writte consent of the partners entitled to receive a major ity of the "distributable net profits", including suc partner, become surety, guarantor, endorser or oth erwise liable for any other person or firm, whethe corporate, sole proprietorship, partnership or oth erwise.

Article VIII.

No partner shall, without the previous writte consent of the remaining partners, assign or hy pothecate his interest in or to this co-partnership or in or to the profits or capital to which said part ner may be entitled.

Any such attempted assignment or hypothecatio shall not, subject, however, to the rights and optio granted to the remaining partners by the provision of Article IX hereof, dissolve the co-partnership nor as against the remaining partners entitle th assignee or the person holding said interest or profi or capital as security during the continuance o this co-partnership, to interfere with or take an part in the management of the co-partnership af fairs or to receive any salary or to require any in formation or account of the co-partnership matter or to inspect the co-partnership books, but it shal merely entitle the said assignee or said other perso to receive in accordance with his contract the profi or capital to which the assigning partner woul otherwise be entitled, in accordance with, at th times and in the amounts as provided by, the cove nants hereof. In the event of any such assignment

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neither the partner so assigning, nor his assignee, shall be entitled to any salary; the partners not so assigning, however, shall be entitled to a reasonable salary in such amount and payable at such times as the said non-assigning partners may from time to time determine.

Article IX.

This co-partnership shall begin on the date hereof and continue for a period of twenty (20) years; provided, however:

(a) In the event that any partner shall, without the previous written consent of the remaining partners, assign or hypothecate his interest in and to this co-partnership, or in any to the profits or capital to which such partner may be entitled, the remaining partners may terminate the interest of such partner in and to the co-partnership and its assets, and are hereby granted the exclusive and irrevocable right and option to purchase the interest of the said partner in and to the co-partnership.

The term of the option, the purchase price, and the manner of payment thereof, shall be as is provided in sub-paragraph (d) of this Article IX.

In the event that the said remaining partners shall not elect to exercise the option hereby granted, the co-partnership shall continue as modified by the provisions of Article VIII hereof, to the expiration of said term.

(b) In the event that any partner hereto shall become mentally incompetent or insane, or in any other way incapable of performing his part of this

Plaintiffs' Exhibit No. 13—(Continued)

co-partnership contract, or shall voluntarily withdraw from the co-partnership, or shall become a bankrupt, or any execution upon any judgment against said partner be levied upon his interest and not released within sixty (60) days or in the event of said partner's interest in and to the co-partnership being charged with the payment of any judgment against, or other obligation of, said partner, the remaining partners hereto may terminate the interest of such partner in and to the co-partnership and its assets and the said remaining partners are hereby granted the exclusive and irrevocable right and option to purchase the interest of such partner in and to the co-partnership.

The term of the option, the purchase price and manner of payment thereof, shall be as is provided in subdivision (d) of this Article IX.

In the event said option be not exercised by said remaining partners, the co-partnership shall continue to the expiration of the original term hereof, excepting only that the said partner violating the foregoing provision shall not be entitled to receive any salary, and the remaining partners shall be entitled to a reasonable salary in such amount and payable at such times as such remaining partners shall determine.

(c) In the event of the death of any partner, the remaining partners may terminate the interest of such deceased partner in and to the co-partnership and the remaining partners are hereby granted an exclusive and irrevocable option to purchase the

Plaintiffs' Exhibit No. 13—(Continued)

interest of such deceased partner in and to the co-partnership.

The terms of the option, the purchase price, and the manner of payment thereof shall be as is provided in subdivision (e) of this Article IX.

In the event that said option shall not be exercised, the co-partnership, as between the surviving partners and the deceased co-partner, shall be deemed dissolved, though not terminated; excepting, however, that the surviving co-partners shall have the right to operate and conduct the co-partnership business and affairs until the expiration of the original term. In the event that the surviving partners shall elect to continue to operate and conduct the co-partnership business and affairs until the expiration of the original term, the interest of the deceased partner, his heirs, executors, administrators, successors and assigns, in and to the "Contributed Capital" and "Earned Capital", profits and losses, shall be reduced in the proportion that the proceeds of the life insurance which shall have been paid for by the co-partnership, as provided by Article X hereof, bears to the total of the "Contributed Capital" and "Earned Capital" of the deceased co-partner, and the interest of each of the surviving co-partners in and to said "Contributed Capital", "Earned Capital", profits and losses, shall be increased in the proportion, and each shall succeed to such proportion as the then interest of each such surviving partner in

Plaintiffs' Exhibit No. 13—(Continued)

the "distributable net profits" bears to the total interests of all of the surviving partners in and to the "distributable net profits". In such event, the surviving partners shall have the exclusive right of conducting, managing and carrying on the business of the co-partnership, and neither the heirs, executors, administrators, or other personal representative of such deceased co-partner shall have any interest whatsoever in and to the business of the co-partnership, or any voice in the management or conduct of the business or affairs of the co-partnership; the only right on the part of such heirs or executors or administrators or other personal representative of such deceased co-partner, shall be to receive the said share of the profits or capital of such deceased co-partner, as reduced, as hereinbefore provided, in accordance with and at the times and in the amounts as provided by the covenants hereof; excepting only, however, that any obligation or liability created or incurred by said surviving partners in the operation of said business shall be binding only upon the surviving partners and the interest of said deceased co-partner, his heirs, executors, administrators, successors and assigns, in and to the co-partnership, but shall not be binding upon nor create any personal obligation or liability upon such heirs, executors, administrators, successors and assigns of said deceased co-partner. In such event, neither the heirs nor executors nor other personal representative of such deceased co-partner shall be entitled to receive any salary; the surviving

Plaintiffs' Exhibit No. 13—(Continued)

partners, however, shall be entitled to receive a reasonable salary in such amount and payable at such times as said surviving partners shall from time to time determine.

(d) In the event of the occurrence of any act giving rise to the right of purchase, as provided by sub-divisions (a) and (b) hereof, and if the partner entitled to exercise said option shall desire to exercise said option, such partner shall give written notice to the partner whose interest is to be purchased, of his intention to exercise said option, said notice to be given within three (3) months after actual knowledge of the event giving rise to said right of purchase.

The purchase price shall be a sum equal to the interest of said partner, (whose interest is to be purchased), in the "Contributed Capital" and in the "Earned Capital", and any other debt owing to such co-partner on the part of the co-partnership; all as shall be shown by a certified audit to be made by the then accountants of the co-partnership, in accordance with the usual accounting practices theretofore followed by the co-partnership, as of the end of the calendar month preceding, or the commencement of the calendar month succeeding, whichever shall be the shortest period from the occurrence of the act giving rise to the right of purchase.

The said purchase price shall be payable as follows, to-wit:

(1) The purchasing partner shall, immediately

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after service of said notice of intention to exercise said option, cause an escrow to be opened in the escrow department of any national trust and savings bank within the City of Los Angeles; said escrow shall be between the said purchasing partner and said partner whose interest is to be purchased.

(2) The purchasing partner shall deposit in said escrow at the time of the opening thereof, a sum equal to twenty-five (25%) per cent of said purchase price, together with a non-negotiable note of said purchasing partner, wherein the said partner whose interest is to be purchased shall be the payee, the amount of said note to be in the amount of the balance of the said purchase price; said note shall be payable in not more than six (6) semi-annual equal installments, together with interest at the rate of four (4%) per cent per annum upon the unpaid balances from time to time; said escrow may provide that the said purchase price shall only be paid over unto the said partner whose interest is to be purchased, or the person entitled thereto, when there shall be transferred unto the purchasing partner the right, title, interest and estate of the partner whose interest is to be purchased in and to the said co-partnership and its assets, free and clear of and from the event or act giving rise to the right of purchase. The purchasing partner shall in any event assume and agree to pay all liabilities of the co-partnership and to forever indemnify and save harmless the partner whose

Plaintiffs' Exhibit No. 13—(Continued)

interest is to be purchased from any loss by reason thereof.

(3) Upon the opening of said escrow and the payment therein of the said sum and the deposit therein of said note, as hereinbefore in paragraph (2) provided, the interest of the partner whose interest is being purchased thereby shall terminate and cease and the partner exercising the said rights and option shall succeed to all of the right, title, interest and estate of the said partner whose interest is thereby being purchased, in and to the said co-partnership assets, free and clear from the event or act giving rise to the right of purchase.

(e) In the event of the occurrence of death of one of the co-partners, giving rise to the right of purchase under sub-paragraph (c) of this Article, and if the surviving partners shall desire to exercise said option, said partners shall give written notice of their intention to exercise said option to the executors or administrators or surviving spouse or other personal representative of such deceased partner within six (6) months from the occurrence of the event giving rise to said right of purchase, or the appointment and qualification of the executor, administrator, or other personal representative of such deceased partner, and written notice thereof served upon the surviving partners, whichever shall last occur.

The purchase price shall be the following sum to-wit:

(1) A sum equal to the interest of such deceased

Plaintiffs' Exhibit No. 13—(Continued)

partner in and to the "Contributed Capital", and in and to the "Earned Capital", and any other debt owing to such co-partner on the part of the co-partnership; all as shall be shown by a certified audit to be made by the then accountants of the co-partnership, in accordance with the usual accounting practices theretofore followed by the co-partnership, as of the end of the calendar month preceding, or the commencement of the calendar month succeeding, whichever shall be the shortest period from, the date of death of the deceased co-partner, less the amount of the proceeds of the life insurance in force and effect payable to the beneficiaries designated by such deceased partner, which said insurance shall have been taken out and the premiums thereon paid by the co-partnership, as provided by Article X hereof. In the event that the amount of said insurance shall exceed the said purchase price, the co-partnership shall have no claim, right, title, interest or estate whatsoever in and to said excess of said insurance, but no further sum shall be payable to the estate, heirs, executors, administrators, or other personal representatives or successors of such deceased co-partner, and his interest in and to the said co-partnership, its assets and properties, shall terminate and cease and neither the said heirs or executors or administrators or other personal representatives of such deceased co-partner shall have any right, title, interest or estate whatsoever in and to the co-partnership or its assets, and in such event, each of the surviving

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partners shall, ipso facto, succeed to the interest of such deceased co-partner in and to the "Contributed Capital" and "Earned Capital" and other debt owing to said co-partner, and in and to the profits and losses, in the proportion as the then interest of each such surviving partner in the "distributable net profits" bears to the total interest of all of the surviving partners in and to the "distributable net profits".

In the event that the amount of said insurance shall be less than the said purchase price as hereinbefore provided, the difference between the said purchase price and the said insurance shall be payable as follows:

a. The purchasing partner shall, immediately after service of said notice of exercise of option, cause an escrow to be opened in the escrow department of any national trust and savings bank in the City of Los Angeles; said escrow shall be between the said purchasing partner and whomsoever may be entitled to receive the said purchase price; the purchasing partner shall deposit in the said escrow at the time of opening thereof, a sum equal to twenty-five (25%) per cent of said difference, together with a negotiable note of said purchasing partner for the balance, which said note shall be payable in not more than six (6) semi-annual equal installments, together with interest at the rate of four (4%) per cent upon the unpaid balances from time to time; interest payable monthly; said note shall by its terms provide that in the event that the

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maker shall default in the payment of any installment of interest or principal when due, or in the event that the maker shall, prior to the payment in full thereof, sell his interest in or withdraw from said co-partnership, or die, or in the event that said co-partnership, as between and among the surviving partners, shall be dissolved, or shall liquidate, or shall sell all or substantially all of its assets, then and in any of said events, the holder of said note may declare the entire balance immediately due and payable; and said note shall further provide by its terms that in the event of any action being brought thereon the maker agrees to pay a reasonable attorney's fee. The escrow may provide that the said purchase price shall only be payable by the said escrow holder when it shall hold for the purchasing partner a good and sufficient release and quitclaim from the person or persons entitled to receive said purchase price together with a warranty bill of sale or other document necessary to vest title in said purchasing partner of all of the interest of such deceased partner in and to the said co-partnership, its properties and assets, subject to its liabilities.

(f) In determining the purchase price under any of the foregoing provisions of this Article IX, no value shall be set upon, and no provision shall be made for, the goodwill, if any, of the co-partnership.

(g) In paying the purchase price under any of the foregoing sub-paragraphs of this Article, the purchasing partners may use any funds of the said

Plaintiffs' Exhibit No. 13—(Continued)

co-partnership to which the partner whose interest is to be purchased would otherwise be entitled.

(h) In the event that there shall be more than one partner entitled to exercise the option granted by subparagraphs (a) or (b) or (c) of this Article, each shall have the right and option to purchase such proportion of the interest of the partner whose interest is to be purchased as the interest of each of the said purchasing partners in and to the "distributable net profits" bears to the total interest of all of the said purchasing partners in and to the "distributable net profits". In the event that any partners entitled to exercise said option shall not elect so to do, the remaining partners also so entitled may exercise the option as to the entire interest of the partner whose interest is to be purchased.

(i) Neither the failure to exercise the said options granted by subparagraphs (a) or (b) or (c) of this Article, or the exercise thereof, shall cause a dissolution of this co-partnership as between or among the remaining co-partners.

(j) In the event of the exercise of the options granted by subparagraphs (a) and/or (b) and/or (c) of this Article, the purchasing partner shall in writing assume and agree to pay all obligations of the co-partnership and to forever indemnify and save harmless the partner whose interest is to be purchased, his heirs, executors, administrators, successors and assigns, from any and all loss by reason thereof.

Plaintiffs' Exhibit No. 13—(Continued)

Article X.

The co-partnership may take out and pay all premiums under policies of life insurance upon the lives of any one or more of the co-partners. The principal amount thereof shall be such as shall be determined by the partners.

Such policies shall be payable in favor of such person or persons as the partner upon whose life the policy shall be issued, shall designate.

Such policies shall, if possible, confer upon the co-partnership the right to borrow upon and against said policies the full loan value thereof whenever the partners shall deem it necessary so to do, and in such event, the partnership shall have no liability whatsoever to the partner upon whose life said policy shall issue or to the beneficiary thereunder for the repayment thereof.

Upon the death of any partner, upon whose life a policy of life insurance shall have been taken out as herein provided, the said insurance upon his life shall be paid as far as this co-partnership is concerned, to said named beneficiary. Such payment shall reduce the interest of said deceased co-partner in and to the co-partnership as hereinbefore by the provisions of subparagraphs (c) and (e) of Article IX provided.

Article XI.

1. In the event of the termination of this co-partnership, expressly subject, however, to the provisions of Article IX and particularly subparagraphs (a), (b) and (c) thereof, the liabilities of

Plaintiffs' Exhibit No. 13—(Continued)

the co-partnership as hereinafter in the following division 3 of this Article XI defined, shall be paid or amply provided for in the order and priority as thereby provided.

2. The payment of a debt or liability shall be deemed to have been adequately provided for if the payment thereof shall have been assumed or guaranteed in good faith by one or more financially responsible persons or corporations or other form of business organization, whether a partner hereto or not, and such provision was determined in good faith and with reasonable care by a majority of the then partners hereof to be adequate at the time of any distribution of the assets upon such expiration.

3. The liabilities of the co-partnership shall be paid in the following order and priority, to-wit:

(a) Those owing to creditors other than partners.

(b) Those owing to partners other than for "Contributed Capital", "Earned Capital", or "distributable net profits".

(c) Those owing to partners in respect of "Contributed Capital".

(d) Those owing to partners in respect of "Earned Capital".

(e) Those owing to partners in respect of "distributable net profits".

Article XII.

If at any time during the continuance of this co-partnership, the partners shall deem it necessary or expedient to make any amendment or addition

Plaintiffs' Exhibit No. 13—(Continued)

to or deletion in any article, clause, phrase, paragraph, sentence or word herein contained for the more advantageous or satisfactory management of the co-partnership business, such may be made by any writing executed by a majority of the then partners hereto; provided, however, that at all events, the Party of the First Part during his lifetime must be one of the partners consenting thereto, and in the event of and upon his death during the lifetime of the Party of the Second Part, then by such party, and thereupon such amendment or addition shall have the same force and effect as if the same had been originally embodied in and formed a part of these articles, or, in the event of any deletion, as if the said deletion had not been a part hereof.

Article XIII.

1. Throughout these Articles of Co-partnership, the singular shall include the plural, the plural shall include the singular, the feminine shall include the masculine and neuter gender, and the masculine shall include the feminine and neuter gender.

2. Whenever in these Articles of Co-Partnership it is provided for any act to be done or designated by the co-partners, it refers to and means the then partners entitled to receive a majority of the "distributable net profits".

3. Unless otherwise specifically provided in these Articles of Co-partnership, and subject to the provisions of Article IX hereof, and particularly sub-

Plaintiffs' Exhibit No. 13—(Continued)

paragraphs (a), (b) and (c) thereof, the partners entitled to receive a majority of the "distributable net profits" at said times shall control in all matters requiring the determination of the partners.

Provided, however, if such majority cannot agree, or in the event of an equal division of such co-partnership upon any matter, the Party of the First Part shall have the right, power and authority to make the final and conclusive decision thereon during his lifetime.

4. Any audit that shall be made as provided by any of the provisions of these Articles of Co-Partnership, including by way of specification and not by way of limitation the provisions of Articles IV, V, IX, X and XI, or any division, subdivision or paragraph thereof, shall be conclusive upon each of the partners hereto as to the interest of each partner in and to the "Contributed Capital", and in and to the "Earned Capital", and in and to the "distributable net profits", and as to any obligation owing by the co-partnership to any partner, and as to any other matter, the subject thereof.

5. Any notice by these Articles of Co-partnership authorized to be given, shall be deemed to be duly given if delivered personally to the person to whom it is authorized to be given, or sent by registered mail, postage prepaid, addressed to him at his usual or last known place of abode. Any notice to be given to the co-partnership shall be given to it in writing at its office.

Plaintiffs' Exhibit No. 13—(Continued)

Article XIV.

This co-partnership is formed under the Uniform Partnership Act as now in force in the State of California, being Title X, Division Third, Part IV of the Civil Code of the State of California, and there is incorporated herein and made a part hereof each and all of the provisions thereof; excepting, however, such portions of the provisions thereof as may be inconsistent herewith, in which event, the provisions hereof shall govern; and excepting further that there is expressly excluded herefrom, and each of the partners hereto does hereby expressly waive, the right to rely upon or to claim any rights under or by virtue of the provisions of subdivision (1) of Section 2403 of the Civil Code of the State of California, the provisions of subdivisions (e), (f) and (h) of Section 2412 of said Civil Code of the State of California, and the provisions of Section 2436 of said Civil Code of the State of California.

Article XV.

These Articles of Co-Partnership are executed in as many parts as there are partners hereto, and each of such parts is hereby declared to be an original; all, however, shall constitute but one and the same agreement.

These Articles of Co-Partnership shall be binding upon and inure to the benefit of the heirs, executors, administrators, successors and assigns of each of the parties hereto.

In Witness Whereof, the parties hereto have

Plaintiffs' Exhibit No. 13—(Continued)

hereunto set their hands and seals the day and year first above written.

/s/ By JACK SMITH,
Party of the First Part or First Co-Partner.

/s/ By ROSE MAE SMITH,
Party of the Second Part or Second Co-Partner.

Jack Smith As Original Trustee of the Barbara Ann Smith Trust, a Voluntary Express Trust, in His Representative Capacity.

/s/ By JACK SMITH,
Party of the Third Part or Third Co-Partner.

Rose Mae Smith As Original Trustee of the Howard Samuel Smith Trust, a Voluntary Express Trust, in Her Representative Capacity.

/s/ By ROSE MAE SMITH,
Party of the Fourth Part or Fourth Co-Partner.

State of California,
County of Los Angeles—ss.

On this 1st day of October, 1943, before me, the undersigned, a Notary Public in and for said County and State, personally appeared Jack Smith, Rose Mae Smith, Jack Smith as Original Trustee

Plaintiffs' Exhibit No. 13—(Continued)

of the Barbara Ann Smith Trust, a Voluntary Express Trust, in his representative capacity and Rose Mae Smith as Original Trustee of the Howard Samuel Smith Trust, a Voluntary Express Trust, in her representative capacity, known to me to be the persons whose names are subscribed to the foregoing instrument, and acknowledged to me that they executed the same.

Witness my hand and official seal.

[Seal] GERTRUDE HARRIS,
Notary Public in and for said County and State.

PLAINTIFFS' EXHIBIT No. 14

SUPPLEMENT TO ARTICLES OF CO-PARTNERSHIP OF BOSTON SHOE COMPANY

This Supplement to Articles of Co-Partnership of Boston Shoe Company, made and entered into as of the first day of October, 1943, by and between Jack Smith, sometimes hereinafter referred to as "Party of the First Part" or "First Co-Partner"; Rose Mae Smith, sometimes hereinafter referred to as "Party of the Second Part" or "Second Co-Partner"; Jack Smith as Original Trustee of the Barbara Ann Smith Trust, a Voluntary Express Trust, in his representative capacity, sometimes hereinafter referred to as "Party of the Third Part" or "Third Co-Partner", and Rose Mae Smith, as Original Trustee of the Howard Samuel Smith

Plaintiffs' Exhibit No. 14—(Continued)

Trust, a Voluntary Express Trust, in her representative capacity, sometimes hereinafter referred to as "Party of the Fourth Part" or "Fourth Co-Partner";

Witnesseth:

Whereas, the parties hereto did heretofore, and as of the First day of October, 1943, enter into "Articles of Co-Partnership"; and

Whereas, it is provided by Division 2 of Article V thereof that there shall be paid to each of the partners thereto who shall render services unto the business of the co-partnership, a salary of such amount and payable at such times as shall be determined by the partners, any such salary to be charged as a part of the cost of doing business of said co-partnership and not an advance or charge against the share of the "distributable net profits" to which such partner so receiving said salary is otherwise entitled; and

Whereas, Party of the First Part and Party of the Second Part are, and will be, rendering services unto the business of said co-partnership and the parties are therefore desirous of agreeing as to the salaries to be paid unto Party of the First Part and Party of the Second Part for the remainder of the calendar year of 1943;

Now, Therefore, It Is Hereby Agreed:

I.

That there shall be paid unto Jack Smith for the remainder of the calendar year of 1943, for his

Plaintiffs' Exhibit No. 14—(Continued)

services unto the business of said co-partnership, a salary based upon the sum of Twenty-five Thousand Dollars ($25,000.00) per calendar year; and there shall be paid unto Rose Mae Smith, for her services unto the business of said co-partnership, for the balance of the calendar year of 1943, a salary based upon the sum of Twenty-Four Hundred Dollars ($2,400.00) per calendar year.

II.

This Supplement to Articles of Co-Partnership is executed in four parts; each part is hereby declared to be an original; all however, shall constitute but one and the same agreement.

This Supplement to Articles of Co-Partnership shall be binding upon and inure to the benefit of the heirs, executors, administrators, successors and assigns of each of the parties hereto.

In Witness Whereof the parties hereto have hereunto set their hands and seals as of the day and year first above written.

/s/ By JACK SMITH,
Party of the First Part
/s/ By ROSE MAE SMITH,
Party of the Second Part

Jack Smith as Original Trustee of the Barbara Ann Smith Trust, a Voluntary Express Trust
/s/ By JACK SMITH,
Party of the Third Part

Plaintiffs' Exhibit No. 14—(Continued)

Rose Mae Smith as Original Trustee of the Howard Samuel Smith Trust, a Voluntary Express Trust

By .....,

Party of the Fourth Part

PLAINTIFFS' EXHIBIT No. 15

ARTICLES OF CO-PARTNERSHIP OF BOSTON SHOE COMPANY

These Articles of Co-Partnership executed as of the 1st day of January, 1945, by and between Jack Smith, sometimes hereinafter referred to as "Party of the First Part" or "First Co-Partner", Rose Mae Smith, sometimes hereinafter referred to as "Party of the Second Part" or "Second Co-Partner", Jack Smith, As Original Trustee of the Barbara Ann Smith Trust, a Voluntary Express Trust, in his representative capacity, sometimes hereinafter referred to as "Party of the Third Part", or "Third Co-Partner", Rose Mae Smith, As Original Trustee of the Howard Samuel Smith Trust, a Voluntary Express Trust, in her representative capacity, sometimes hereinafter referred to as "Party of the Fourth Part" or "Fourth Co-Partner" and Herman Weishaupt, sometimes hereinafter referred to as "Party of the Fifth Part" or "Fifth Co-Partner";

Plaintiffs' Exhibit No. 15—(Continued)

Witnesseth:

Whereas, Party of the First Part, Party of the Second Part, Party of the Third Part and Party of the Fourth Part were heretofore and unto the close of business on the 31st day of December, 1944, co-partners doing business under the firm name and style of Boston Shoe Company, with their principal place of business at 826 South Los Angeles Street, City and County of Los Angeles, State of California, under certain "Articles of Co-Partnership" executed as of the 1st day of October, 1943; and

Whereas, Party of the Fifth Part is desirous of becoming associated with the remaining parties hereto as a co-partner for the ownership and operation of said business and the remaining parties hereto being agreeable thereto, all of the parties hereto are desirous of constituting themselves into a co-partnership upon the terms, conditions and covenants as herein set forth, supplementing these "Articles of Co-Partnership" only as hereinafter in Article XV provided by certain only of the provisions of the Uniform Partnership Act of the State of California.

Now, Therefore, It Is Hereby Agreed:

I.

The Co-Partnership heretofore existing among Party of the First Part, Party of the Second Part, Party of the Third Part and Party of the Fourth Part be and the same is hereby dissolved and terminated as of the close of business on the 31st day

Plaintiffs' Exhibit No. 15—(Continued)

of December, 1944. The interest of each of said parties in and to the assets thereof and the obligations and liabilities on the part of said co-partnership unto each thereof, shall be more particularly set forth in a "Balance Sheet of Boston Shoe Company, a Co-Partnership, as of the close of business on December 31st, 1944" to be prepared by Meyer Pritkin & Co., Certified Public Accountants and Accountants for said co-partnership; said Balance Sheet, together with the Profit and Loss Statement for the period ending December 31st, 1944, which said Profit and Loss Statement shall likewise be prepared by Meyer Pritkin & Co., is hereby agreed to constitute the final accounting of the Co-Partnership heretofore existing among the said Party of the First Part, Party of the Second Part, Party of the Third Part and Party of the Fourth Part, and any other or further accounting is hereby waived.

Article II.

The parties hereto do hereby agree that they are, from this time on, for the term, upon the conditions, covenants and agreements hereof, co-partners.

Article III.

1. The Co-Partnership hereby created shall be conducted and carried on under the partnership name and style of "Boston Shoe Company".

The name "Boston Shoe Company" and all other trade names and trade-marks heretofore used by the Co-Partnership heretofore existing among the

Plaintiffs' Exhibit No. 15—(Continued)

Party of the First Part, Party of the Second Part, Party of the Third Part and Party of the Fourth Part, and all other trade names and trade-marks which shall hereafter be used by this Co-Partnership, created by these Articles of Co-Partnership are and shall continue to be and those hereafter used shall become and be the property of Party of the First Part, Party of the Second Part, Party of the Third Part and Party of the Fourth Part said parties hereby licensing this Co-Partnership to use all of said trade names and trade-marks until the dissolution hereof; neither the Co-Partnership created hereby nor Party of the Fifth Part shall hereby nor hereafter acquire any right, title, interest or estate therein other than the right on the part of the Co-Partnership created hereby to use said trade-marks and trade names until the dissolution hereof, excepting only, in the event of the death of the last to die of Party of the First Part and Party of the Second Part, in which event the interest of said parties in and to said trade-marks and trade names shall be deemed an asset and property within the provisions of Article X, Division (c) thereof.

2. The principal place of business of this Co-Partnership shall be at Number 826 South Los Angeles Street, City of Los Angeles, County of Los Angeles, State of California, or at such other place as the partners hereto may from time to time designate in writing.

This partnership may have one or more offices

Plaintiffs' Exhibit No. 15—(Continued)

and in any state or territory of the United States, as may be determined and designated in writing by the partners hereto.

Article IV.

1. The business of this Co-Partnership shall be to buy, sell, manufacture and deal in, and to engage in and conduct and carry on the business of buying, selling, manufacturing and dealing in footwear and any other business related thereto and deemed to be for the best interests of the Co-Partnership.

2. In general, this Co-Partnership may carry on any business that may be carried on by, and have and exercise all powers that a natural person may regularly carry on or have under the laws of the State of California.

Article V.

1. The capital of the Co-Partnership shall consist of the following, to-wit:

(A) Party of the First Part, Party of the Second Part, Party of the Third Part and Party of the Fourth Part do hereby sell, assign, transfer, set over and convey unto this Co-Partnership, subject to the provisions and limitations of Article III, Division 1 hereof, all property, whether real, personal or mixed and of whatsoever type, nature, kind and description, including leases and leaseholds owned by said parties in undivided interests as tenants in common in that certain Co-Partnership

Plaintiffs' Exhibit No. 15—(Continued)

business formerly and until the close of business on the 31st day of December, 1944, existing between them, under the firm name and style of Boston Shoe Company, subject to the liabilities to which said assets are subject, all as shall be shown upon a "Statement of Assets and Liabilities of Boston Shoe Company as of the close of business on December 31st, 1944", to be prepared by Meyer Pritkin & Co. The total net capital of said business as of the close of business on said 31st day of December, 1944, as shall be shown upon said "Statement of Assets and Liabilities of Boston Shoe Company as of the close of business on December 31st, 1944", which said statement of assets and liabilities shall be conclusive and binding upon all of the parties hereto, Parties of the First Part, Second Part, Third Part and Fourth Part do guarantee will not be less than the total sum of Two Hundred Thousand ($200,000.00) Dollars. In the event that the said total net capital of all of said Parties of the First Part, Second Part, Third Part and Fourth Part shall be less than said sum of Two Hundred Thousand ($200,000.00) Dollars, each of said parties, to wit, Party of the First Part, Party of the Second Part, Party of the Third Part and Party of the Fourth Part shall add to the interest of each such amount as may be necessary to make the capital interest of each of said parties equal to the sum hereinafter in this paragraph set forth. In the event that the total net capital of said business shall exceed said sum of Two Hundred Thou-

Plaintiffs' Exhibit No. 15—(Continued)

sand ($200,000.00) Dollars, as shall be shown by said statement of assets and liabilities the interest of each of said parties therein in excess of the amounts hereinafter in this paragraph set forth shall be deemed a loan by said Party unto this Co-Partnership to be repaid at such time and to bear such rate of interest, if any, as the partners hereto shall agree. By reason of the foregoing, the interest of each of the parties of the said First Part, Second Part, Third Part and Fourth Part therein is valued at and the contribution of each to the invested capital of this Co-Partnership is, therefore, agreed to be as follows:

Jack Smith: $80,000.00.

Rose Mae Smith: $60,000.00.

Jack Smith, Original Trustee of the Barbara Ann Smith Trust, a Voluntary Express Trust: $30,000.00.

Rose Mae Smith, Original Trustee of the Howard Samuel Smith Trust, a Voluntary Express Trust: $30,000.00.

The phrase "net capital" as herein used is hereby defined to mean the residue of the book values of the assets of said Boston Shoe Company, after deducting and making provisions for the payment of all liabilities of said business as disclosed by the books and records thereof existing as of the close of business on the 31st day of December, 1944, without, however, any provisions for goodwill, the parties hereto hereby agreeing that said business had no goodwill. The amounts, if any, owing by

Plaintiffs' Exhibit No. 15—(Continued)

this Co-Partnership unto the said Parties of the First Part, Second Part, Third Part and Fourth Part by reason of the interest of each being in excess of the agreed invested capital of each, shall be set forth in the ledgers of this Co-Partnership by the accountants hereof, Messrs. Meyer Pritkin & Co., and such entries shall be conclusive and binding upon all of the parties hereto.

(B) Party of the Fifth Part shall contribute unto the invested capital hereof the sum of Twenty-Two Thousand ($22,000.00) Dollars.

(C) Upon the close of the first fiscal year, or calendar year, whichever may be used by this Co-Partnership for its purposes, and thereafter upon the close of each fiscal or calendar year, as the case may be, an audit shall be made of the business of the Co-Partnership, and all net profits of the Co-Partnership earned and collected shall be thereby determined. No provision shall be made in any audit of the goodwill, if any, of the Co-Partnership. In the event that such audit shall show a net profit earned and collected for such "accounting period", and before any distribution of net profits shall be made to any partner, there shall be first set aside to capital such percentage of said net profits as the partners shall from time to time determine. Said capital so created shall be used as capital of the Co-Partnership in the operation of the Co-Partnership business. The net profits remaining after setting aside said percentage to said capital are some-

Plaintiffs' Exhibit No. 15—(Continued)

times hereinafter referred to as "distributable net profits".

The said period of each audit is sometimes herein in these Articles of Co-Partnership referred to as "accounting period".

Each partner shall have an interest in the capital created by the foregoing provision in the same proportion to which each partner shall share in the losses of the Co-Partnership, as provided in Article VII hereof.

(D) If at any time or times hereafter further capital be required for carrying on the Co-Partnership business and the partners shall determine to increase the capital, the additional capital shall be advanced by the partners in the same proportion as they are entitled to share in the "distributable net profits".

Article VI.

1. The net profits of the Co-Partnership shall be distributed as follows:

(A) There shall be first set aside to capital such percentage of the net profits as is provided for by Subdivision C of Article V hereof.

(B) To Jack Smith, thirty-six (36%) per cent of the "distributable net profits".

(C) To Rose Mae Smith, twenty-seven (27%) per cent of the "distributable net profits".

(D) To Jack Smith, As Original Trustee of the Barbara Ann Smith Trust, a Voluntary Express Trust, in his representative capacity, thirteen and

Plaintiffs' Exhibit No. 15—(Continued)

one-half (13½%) per cent of the "distributable net profits".

(E) To Rose Mae Smith, As Original Trustee of the Howard Samuel Smith Trust, a Voluntary Express Trust, in her representative capacity, thirteen and one-half (13½%) per cent of the "distributable net profits".

(F) To Herman Weishaupt, ten (10%) per cent of the "distributable net profits".

2. There shall be paid to each of the partners hereto who shall render services unto the business of the Co-Partnership, a salary of such amount and payable at such times as shall be determined by the partners hereto.

Any salary received by any partner under any provision of these "Articles of Co-Partnership" shall be deemed and charged as a part of the cost of doing business of this Co-Partnership, and not an advance or charge against the share of the "distributable net profits" to which such partner so receiving said salary is otherwise entitled.

Until further agreement of the partners hereto, there shall be paid unto the following partners the following salaries, to wit:

Jack Smith, Twenty-Five Thousand ($25,000.00) Dollars per annum;

Rose Mae Smith, Twenty-Four Hundred ($2,400.00) Dollars per annum;

Herman Weishaupt, Six Thousand ($6,000.00) Dollars per annum.

3. Each partner shall be entitled to draw out of

Plaintiffs' Exhibit No. 15—(Continued)

and from the "distributable net profits" and/or Capital of the Co-Partnership for his own special account, such amount as the co-partners hereto may from time to time designate.

4. If any partner shall leave in the business, after any accounting periods, any share of such partner's "distributable net profits" other than the percentage to be set aside to the capital, and other than in pursuance of an agreement among the partners to increase proportionately, that is in the same proportion that each is liable for losses hereof, the capital, the same shall be considered a debt unto such co-partner. No interest shall be payable thereon.

5. If any partner shall advance to the Co-Partnership at its request any sums, it shall be deemed a debt owing unto such co-partner on the part of the Co-Partnership. Interest shall be payable thereon of such rate as the partners hereto may from time to time agree.

Article VII.

Each of the partners hereto shall share in the losses of the Co-Partnership in the same proportion that each is entitled to share in the "distributable net profits".

Article VIII.

1. Party of the Fifth Part shall devote his entire business time to the business of the Co-Partnership; the remaining partners hereto need only devote so much of their time unto the business of

Plaintiffs' Exhibit No. 15—(Continued)

the Co-Partnership as the remaining co-partners shall in their absolute, arbitrary and uncontrolled discretion deem necessary or proper.

2. Books of account shall be kept and entries made therein of all monies, goods, checks, receipts, payments, and all transactions of the Co-Partnership. Said books of account shall be kept where the business of the Co-Partnership is to be carried on, and shall be at all times open to the examination of the partners, or either or any of them.

3. All monies of the Co-Partnership shall be deposited in a bank account and in the name of the Co-Partnership. All withdrawals therefrom, checks upon or drafts against said account must be and need only be signed by either Party of the First Part or any two of the remaining partners.

4. The Co-Partnership business shall be managed and carried on, and all contracts, deals or transactions given or taken for any matter or thing concerning the Co-Partnership, shall be made, given or taken and entered into in the name of the Co-Partnership.

5. Excepting only Party of the First Part, none of the remaining partners shall, during the continuance of this Co-Partnership, carry on or be concerned or interested financially, directly or indirectly, in the same kind of business as that carried on by this Co-Partnership, nor be engaged in nor undertake, during the existence hereof, any other trade or business.

6. No partner hereto shall, without the written

Plaintiffs' Exhibit No. 15—(Continued)

consent of the partners entitled to receive a majority of the "distributable net profits", including such partner, become surety, guarantor, endorser or otherwise liable for any other person or firm, whether corporate, sole proprietorship, partnership or otherwise.

Article IX.

No partner shall, without the previous written consent of the remaining partners, assign or hypothecate his interest in or to this Co-Partnership, or in or to the profits or capital to which said partner may be entitled.

Any such attempted assignment or hypothecation shall not, subject, however, to the rights and option granted to the remaining partners by the provisions of Article X hereof, dissolve the Co-Partnership, nor as against the remaining partners entitle the assignee or the person holding said interest or profit or capital as security during the continuance of this Co-Partnership, to interfere with or take any part in the management of the Co-Partnership affairs or to receive any salary or to require any information or account of the Co-Partnership matters or to inspect the Co-Partnership books, but it shall merely entitle the said assignee or said other person to receive in accordance with his contract the profit or capital to which the assigning partner would otherwise be entitled, in accordance with, at the times and in the amounts as provided by, the covenants hereof. In the event of any such assignment, neither the partner so assigning, nor

Plaintiffs' Exhibit No. 15—(Continued)

his assignee, shall be entitled to any salary; the partners not so assigning, however, shall be entitled to a reasonable salary in such amount and payable at such times as the said non-assigning partners may from time to time designate.

Article X.

This Co-Partnership shall begin on the 1st day of January, 1945, and continue for an original term of three (3) years and thereafter for successive and continuous minimum terms of two (2) years each. In the event that any partner shall desire to dissolve this Co-Partnership, he shall give notice of his election to dissolve this Co-Partnership at least ninety (90) days prior to the expiration of the then existing term; such notice shall only be effective upon the expiration of the then existing term. If no partner shall give such notice, this partnership shall continue for another term of two years and thereafter for successive, and continuous and minimum terms of two years each, unless and until any partner hereto shall give said notice. Provided, however;

(a) In the event that any partner shall, without the previous written consent of the remaining partners entitled, with such partner, to a majority of the net distributable profits, or assigns or hypothecates his or her interest in and to this Co-Partnership, or in and to the profits or capital to which such partner may be entitled, the remaining partners, other than Party of the Fifth Part, may

Plaintiffs' Exhibit No. 15—(Continued)

terminate the interest of such partner in and to the Co-Partnership and its assets, and are hereby granted the exclusive and irrevocable right and option to purchase the interest of the said partner in and to the Co-Partnership.

The term of the option, the purchase price, and the manner of payment thereof, shall be as is provided in division (d) of this Article X.

In the event that the said remaining partners shall not elect to exercise the option hereby granted, the Co-Partnership shall continue as modified by the provisions of Article IX hereof, to the expiration of the then existing term.

(b)

(1) In the event that any partner hereto shall become mentally incompetent or insane or in any other way incapable of performing his part of this Co-Partnership contract, or shall voluntarily withdraw from the Co-Partnership, or shall become bankrupt, or any execution upon any judgment against said partnership be levied upon his interest and not released within sixty days, or, in the event of said partner's interest in and to the Co-Partnership being charged with the payment of any judgment against or other obligation of said partner, or in the event that Party of the Fifth Part shall become ill and such illness shall prevent him from performing his duties as a co-partner for a period of sixty (60) consecutive days or an aggregate of one hundred twenty (120) days in any one calendar year, or shall become in any way incapable of per-

Plaintiffs' Exhibit No. 15—(Continued)

forming his part of this Co-Partnership contract or in the event that said Party of the Fifth Part shall elect or attempt to dissolve or terminate this Co-Partnership or shall bring any proceedings for the dissolution or termination hereof, then and in either or any of said events, the remaining partners hereto, other than Party of the Fifth Part and irrespective whether caused by the fault, wrong, negligence or otherwise of said remaining partners, any or either thereof may terminate the interest of such partner in and to the Co-Partnership and its assets and the said remaining partners, other than the said Party of the Fifth Part, are hereby granted an exclusive and irrevocable right and option to purchase the interest of said co-partner in and to the Co-Partnership.

(2) The term of the option under the foregoing subdivision (1), the purchase price and manner of payment thereof shall be as is provided in the following division (d) of this Article X.

(3) In the event that the option under the foregoing subdivision (1) be not exercised by the said remaining partners, the Co-Partnership shall continue to the expiration of the then existing term hereof, excepting only that the partner violating the provisions hereof shall not be entitled to receive any salary and the remaining partners shall be entitled to a reasonable salary in such amount and payable at such times as said remaining parties shall determine.

Plaintiffs' Exhibit No. 15—(Continued)

(c)

(1) In the event of the death of any party hereto, the remaining partners, including said Party of the Fifth Part, may terminate the interest of such deceased partner in and to the Co-Partnership and the remaining parties, including said Party of the Fifth Part, are hereby granted an exclusive and irrevocable option to purchase the interest of such deceased partner in and to the Co-Partnership and its assets.

The term of the option under the foregoing paragraph, the purchase price and the manner of payment thereof shall be as is provided in division (d) of this Article X.

(2) In the event that the option granted under the foregoing subdivision (1) of this division (c) shall not be exercised, the Co-Partnership, as between the surviving partners and the deceased co-partner, shall be deemed dissolved, though not terminated; excepting, however, that the surviving co-partners shall have the right to operate and conduct the Co-Partnership business and affairs until the expiration of the then existing term hereof. In the event that the surviving partners shall elect to continue to operate and conduct the Co-Partnership business and affairs until the expiration of the then existing term hereof, the interest of the deceased partner, his heirs, executors, administrators, successors and assigns, in and to the capital and profits and losses, shall be reduced in the proportion that the proceeds of the life insurance, if any, the pre-

Plaintiffs' Exhibit No. 15—(Continued)

miums of which shall have been paid for by the Co-Partnership, as provided by Article XI hereof, bears to the total of the capital of such deceased co-partner and the interest of each of the surviving co-partners in and to the capital and in and to the profits and losses, shall be increased in the proportion and each shall succeed to such proportion as the then interest of each such surviving partner in the "distributable net profits" bears to the total interest of all of the surviving partners in and to the "distributable net profits". In such event, the surviving partners shall have the exclusive right of conducting, managing and carrying on the business of the Co-Partnership, and neither the heirs, executors, administrators, or other personal representative of such deceased co-partner shall have any interest whatsoever in and to the business of the Co-Partnership, or any voice in the management or conduct of the business or affairs of the Co-Partnership; the only right on the part of such heirs or executors or administrators or other personal representative of such deceased co-partner, shall be to receive the said share of the profits or capital of such deceased co-partner, as reduced, as hereinbefore provided, in accordance with and at the times and in the amounts as provided by the covenants hereof; excepting only, however, that any obligation or liability created or incurred by said surviving partners in the operation of said business shall be binding only upon the surviving partners and the interest of said deceased co-partner, his

Plaintiffs' Exhibit No. 15—(Continued)

heirs, executors, administrators, successors and assigns, in and to the Co-Partnership, but shall not be binding upon nor create any personal obligation or liability upon such heirs, executors, administrators, successors and assigns of said deceased co-partner. In such event, neither the heirs nor executors nor other personal representative of such deceased co-partner shall be entitled to receive any salary; the surviving partners, however, shall be entitled to receive a reasonable salary in such amount and payable at such times as said surviving partners shall from time to time determine.

(d)

(1) In the event of the occurrence of any act giving rise to the right of purchase as provided by the foregoing divisions (a) and/or (b) and/or (c) hereof, and if a partner entitled to exercise said option shall desire to exercise said option, he shall give written notice to the partner whose interest is to be purchased or unto his administrator, executor or other personal representative, of his intention to exercise said option, said notice to be given within three months after actual knowledge of the event giving rise to the right of purchase. Said notice of exercise of option shall be served either personally or by registered mail, postage prepaid, addressed to the party to whom said notice is to be given, at his last known residence or business address and said notice shall be deemed effective either when personally served or when deposited into the United States Mail, in an envelope addressed to

Plaintiffs' Exhibit No. 15—(Continued)

said party to whom said notice is to be given, at his last known residence or business address, postage prepaid, registered, return receipt requested. Said date is sometimes hereinafter designated as the "effective date" of exercise of option.

(2) The purchase price shall be a sum equal to the interest of the partner (whose interest is to be purchased) in the capital and in and to any earned and undistributed profits, if any, and any other debt owing to such co-partner on the part of the Co-Partnership, less any incurred but unpaid losses and if the purchase be by reason of the death of one of the co-partners under the option conferred by the foregoing division (c), less the proceeds of the life insurance, if any, the premiums of which shall have been paid for by the Co-Partnership as provided by Article XI hereof, all as shall be shown by a certified audit to be made by the then accountants of the Co-Partnership in accordance with the usual accounting practices theretofore followed by the Co-Partnership, subject, however, to the definitions and limitations of the following division (e) as of the effective date of the notice of exercise of option; provided, however, that if the purchase be by Party of the First Part and/or Party of the Second Part and/or Party of the Third Part and/or Party of the Fourth Part of the interest of Party of the Fifth Part for any reason other than the death of said Party of the Fifth Part and if the effective date of the notice of exercise of option be a date more than ninety (90) days prior to the ex-

Plaintiffs' Exhibit No. 15—(Continued)

piration of the then existing minimum term, the purchase price of the interest of said Party of the Fifth Part shall be increased by a sum equal to his salary for a period of sixty (60) days as provided by the provisions of division (2) of Article VI hereof.

(3) The purchase price shall be payable as follows, to wit:

(a) The purchasing partner shall, immediately after service of said notice of intention to exercise said option, cause an escrow to be opened in the escrow department of any national trust and savings bank within the City of Los Angeles; said escrow shall be between the said purchasing partner and said partner whose interest is to be purchased.

(b) The purchasing partner shall deposit in said escrow at the time of the opening thereof, a sum believed by him to be equal to twenty-five (25%) per cent of said purchase price.

(c) If the purchase price be of the interest of Party of the Fifth Part and other than in the event of his death, the balance of the purchase price shall be deposited into said escrow within thirty (30) days after receipt of the certified audit hereinbefore provided for.

(d) In all instances, other than as provided by the foregoing subparagraph (c), within a reasonable time after the receipt of the certified audit hereinbefore provided to be made, he shall deposit into said escrow his non-negotiable note wherein the said partner whose interest is to be purchased

Plaintiffs' Exhibit No. 15—(Continued)

shall be the payee, the amount of said note to be in the amount of the balance of the said purchase price; said note shall be payable in not more than six (6) quarterly equal installments, together with interest at the rate of four (4%) per cent per annum upon the unpaid balances from time to time, interest payable quarterly; said note shall by its terms provide that in the event that the maker shall default in the payment of any installment of interest or principal when due, or in the event that the maker shall, prior to the payment in full thereof, sell his interest in or withdraw from said co-partnership, or die, or in the event that said Co-Partnership, as between and among the surviving partners shall be dissolved, or shall liquidate, or shall sell all or substantially all of its assets, then and in any of said events, the holder of said note may declare the entire balance immediately due and payable; and said note shall further provide by its terms that in the event of any action being brought thereon the maker agrees to pay a reasonable attorney's fee. Said escrow may provide that the said purchase price shall only be paid over unto the said partner whose interest is to be purchased, or the person entitled thereto, when there shall be transferred unto the purchasing partner the right, title, interest and estate of the partner whose interest is to be purchased in and to the said Co-Partnership and its assets, free and clear of and from the event or act giving rise to the right of purchase.

Plaintiffs' Exhibit No. 15—(Continued)

(e) Upon opening of said escrow and the payment therein of the said sum, and the deposit therein of said note as hereinbefore in the foregoing subparagraphs provided, or the deposit of the balance of the purchase price as in the said subparagraphs provided, if the purchase be of the interest of Party of the Fifth Part other than by reason of his death, the interest of the partner whose interest is being purchased thereby shall terminate and cease and the partner exercising the said rights and option shall succeed to all of the right, title, interest and estate of the said partner whose interest is thereby being purchased, in and to the Co-Partnership and its assets, free and clear of and from the event or act giving rise to the right of purchase as of the effective date of the notice of exercise of option.

(e) In determining the purchase price under any of the foregoing provisions of this Article X: No value shall be set upon and no provision shall be made for the goodwill, if any, of the Co-Partnership; no value shall be set upon any of the trade names, trade-marks, leaseholds, leasehold improvements and fixtures, unless any value thereof be set forth upon the books of the Co-Partnership; all stock in trade shall be valued at its cost or replacement value or market value, whichever is the lower, less ten (10%) per cent; all other assets shall be by the accountants valued at book value.

(f) In paying the purchase price under any of the foregoing subdivisions of this Article, the pur-

Plaintiffs' Exhibit No. 15—(Continued)

chasing partners may use any funds of the said Co-Partnership to which the partner whose interest is to be purchased would otherwise be entitled.

(g) In the event that there shall be more than one partner entitled to exercise the option granted by divisions (a) and/or (b) and/or (c) of this Article, each shall have the right, option or duty to purchase said proportion of the interest of the partner whose interest is to be purchased as the interest of each of said purchasing partners in and to the "distributable net profits" bears to the total interest of all of said purchasing partners in and to the "distributable net profits". In the event that any partner entitled to exercise said option shall not elect so to do, the remaining partners also so entitled may exercise said option as to the entire interest of the partner whose interest is to be purchased.

(h) Neither the failure to exercise the said options granted by subdivisions (a) and/or (b) and/or (c) of this Article, or the exercise thereof, shall cause a dissolution of this Co-Partnership as between or among the remaining partners.

(i) In the event of the exercise of the options granted by subdivisions (a) and/or (b) and/or (c) of this Article, the purchasing partner shall in writing assume and agree to pay when due, all obligations of the Co-Partnership scheduled in the Certified Audit hereinbefore provided to be made and shall agree to forever indemnify and save harmless the partner whose interest is to be pur-

Plaintiffs' Exhibit No. 15—(Continued)

chased, his heirs, executors, administrators, successors and assigns, from any and all loss by reason thereof.

Article XI.

The Co-Partnership may take out and pay all premiums under policies of life insurance upon the lives of any one or more of the co-partners. The principal amount thereof shall be such as shall be determined by the partners.

Such policies shall be payable in favor of such person or persons as the partner upon whose life the policy shall be issued shall designate.

Such policies shall, if possible, confer upon the Co-Partnership the right to borrow upon and against said policies the full loan value thereof whenever the partners shall deem it necessary so to do, and in such event, the partnership shall have no liability whatsoever to the partner upon whose life said policy shall issue or to the beneficiary thereunder for the repayment thereof.

Upon the death of any partner, upon whose life a policy of life insurance shall have been taken out as herein provided, the said insurance upon his life shall be paid as far as this Co-Partnership is concerned, to said named beneficiary. In the event that the proceeds of said insurance shall be equal to or exceed the interest of the deceased in and to the Co-Partnership, neither this Co-Partnership nor the remaining co-partners shall have any right, title, interest, estate or claim in, to, upon or against the proceeds of said life insurance, but in such event,

Plaintiffs' Exhibit No. 15—(Continued)

the interest of the said deceased in and to the capital and profits and losses shall terminate and the interest of each of the surviving co-partners in and to the capital and in and to the profits and losses shall be increased in the proportion and each shall succeed to such proportion as the then interest of each surviving partner in the "distributable net profits" bears to the total interest of all of the surviving partners in and to the said "distributable net profits". In the event that the proceeds of said life insurance shall be less than the interest of said deceased in and to the said Co-Partnership, the interest of the said deceased co-partner, his heirs, executors, administrators, successors and assigns in and to the capital and profits and losses shall be reduced in the proportion that the proceeds of the said life insurance, if any, bears to the total of the capital of such deceased co-partner and the interest of each of the surviving co-partners in and to the capital and in and to the profits and losses shall be increased in the proportion and each shall succeed to such proportion thereof as the then interest of each such surviving partner in the "distributable net profits" bears to the total interest of all of the surviving partners in and to the "distributable net profits".

Article XII.

1. In the event of the termination of this Co-Partnership, expressly subject, however, to the provisions of Article X and particularly divisions (a), (b) and (c) thereof, the liabilities of the Co-Part-

Plaintiffs' Exhibit No. 15—(Continued)

nership as hereinafter in the following division 3 of this Article XII defined, shall be paid or amply provided for in the order and priority as thereby provided.

2. The payment of a debt or liability shall be deemed to have been adequately provided for if the payment thereof shall have been assumed or guaranteed in good faith by one or more financially responsible persons or corporations or other form of business organization, whether a partner hereto or not, and such provision was determined in good faith and with reasonable care by a majority of the then partners hereof to be adequate at the time of any distribution of the assets upon such expiration.

3. The liabilities of the Co-Partnership shall be paid in the following order and priority, to wit:

(a) Those owing to creditors other than partners.

(b) Those owing to partners other than for contributed capital, earned capital or distributable net profits.

(c) Those owing to partners in respect of contributed capital.

(e) Those owing to partners in respect of distributable net profits.

Article XIII.

If at any time during the continuance of this Co-Partnership, the partners shall deem it necessary or expedient to make any amendment or addition to or deletion in any article, clause, phrase, paragraph, sentence or word herein contained for the

Plaintiffs' Exhibit No. 15—(Continued)

more advantageous or satisfactory management of the Co-Partnership business, such may be made by any writing executed by the partners entitled to receive a majority of the distributable net profits and thereupon such amendment or addition shall have the same force and effect as if the same had been originally embodied in and formed a part of these articles, or, in the event of any deletion, as if the said deletion had not been a part hereof, excepting only that the salary of Party of the Fifth Part, the subject of Article VI, division (2) and the participation of said party in the net profits the subject of Article VI division (1) and the rights granted unto said party by the provisions of Article X, shall not be affected without his written consent.

Article XIV.

1. Throughout these Articles of Co-Partnership the singular shall include the plural, the plural shall include the singular, the feminine shall include the masculine and neuter gender, and the masculine shall include the feminine and neuter gender.

2. Whenever in these Articles of Co-Partnership it is provided for any act to be done or designated by the co-partners, it refers to and means the then partners entitled to receive a majority of the "distributable net profits".

3. Unless otherwise specifically provided in these Articles of Co-Partnership, and subject to the provisions of Article X hereof, and particularly division (a), (b) and (c) thereof, the partners entitled

Plaintiffs' Exhibit No. 15—(Continued)

to receive a majority of the "distributable net profits" at said times shall control in all matters requiring the determination of the partners.

Provided, however, if such majority cannot agree, or in the event of an equal division of the co-partners upon any matter, the Party of the First Part shall have the right, power and authority to make the final and conclusive decision thereon during his lifetime.

4. Any audit that shall be made as provided by any of the provisions of these Articles of Co-Partnership, including by way of specification and not by way of limitation the provisions of Articles I, V, VI, VIII, X and XII, or any division, subdivision or paragraph thereof, shall be conclusive upon each of the partners hereto as to the interest of each partner in and to the capital and in and to the earned and undistributed profits, if any, and in and to the "distributable net profits" and as to any obligation owing by the Co-Partnership to any partner, and as to any other matter, the subject thereof.

5. Any notice by these Articles of Co-Partnership authorized to be given, shall be deemed to be duly given if delivered personally to the person to whom it is authorized to be given, or sent by registered mail, postage prepaid, addressed to him at his usual or last known place of abode. Any notice to be given to the Co-Partnership shall be given to it in writing at its office.

Plaintiffs' Exhibit No. 15—(Continued)

Article XV.

This Co-Partnership is formed under the Uniform Partnership Act as now in force in the State of California, being Title X, Division Third, Part IV of the Civil Code of the State of California, and there is incorporated herein and made a part hereof each and all of the provisions thereof; excepting, however, such portions of the provisions thereof as may be inconsistent herewith, in which event, the provisions hereof shall govern; and excepting further that there is expressly excluded herefrom, and each of the partners hereto does hereby expressly waive, the right to rely upon or to claim any rights under or by virtue of the provisions of Section 2402, subdivision (1); Section 2403, subdivision (3); Section 2412, subdivisions (a), (e), (f), (h); Section 2427; Section 2431; Section 2436 of the Civil Code of the State of California.

Article XVI.

These Articles of Co-Partnership are executed in as many parts as there are partners hereto, and each of such parts is hereby declared to be an original; all, however, shall constitute but one and the same agreement.

These Articles of Co-Partnership shall be binding upon and inure to the benefit of the heirs, executors, administrators, successors and assigns of each of the parties hereto.

In Witness Whereof, the parties hereto have

Plaintiffs' Exhibit No. 15—(Continued)

hereunto set their hands and seals the day and year first above written.

/s/ By JACK SMITH,
Party of the First Part or First Co-Partner.

/s/ By ROSE MAE SMITH,
Party of the Second Part or Second Co-Partner.

Jack Smith As Original Trustee of the Barbara Ann Smith Trust, a Voluntary Express Trust, in His Representative Capacity.

/s/ By JACK SMITH,
Party of the Third Part or Third Co-Partner.

Rose Mae Smith, As Original Trustee of the Howard Samuel Smith Trust, a Voluntary Express Trust, in Her Representative Capacity.

/s/ By ROSE MAE SMITH,
Party of the Fourth Part or Fourth Co-Partner.

/s/ By HERMAN WEISHAUPT,
Party of the Fifth Part or Fifth Co-Partner.

PLAINTIFFS' EXHIBIT No. 16

AGREEMENT

This Agreement made and executed as of the 2nd day of January, 1948, by, between and among Jack Smith, hereinafter sometimes designated as "Jack", Rose Mae Smith, hereinafter sometimes designated as "Rose", the Barbara Ann Smith Trust, a voluntary express trust, hereinafter sometimes designated as "Barbara Trust", and the Howard Samuel Smith Trust, a voluntary express trust, hereinafter sometimes designated as "Howard Trust",

Witnesseth:

Whereas, "Jack", as Trustor, heretofore created "Howard Trust", for the benefit of Howard Samuel Smith, as primary beneficiary, and "Rose", as Trustor, heretofore created "Barbara Trust" for the benefit of Barbara Ann Smith, as primary beneficiary; and

Whereas, "Jack" is the original Trustee of "Barbara Trust" and "Rose" is the original Trustee of "Howard Trust"; and

Whereas, "Jack", "Rose", "Barbara Trust" and "Howard Trust" are all copartners in and are all of the copartners of Boston Shoe Company, a copartnership, hereinafter sometimes designated as "Co-partnership"; and

Whereas, in the year 1947 the United States Government announced that income which, pursuant to the Articles of the said "Co-partnership", was the income of the respective trusts would nonetheless be treated for tax purposes as though it were

Plaintiffs' Exhibit No. 16—(Continued)

income of respectively "Jack" and "Rose", and assessed deficiencies against "Jack" and "Rose" accordingly; and

Whereas, similar action has been taken by the State of California; and

Whereas, it is contemplated that "Jack" and "Rose", for the benefit of the respective trusts, will seek a refund of such taxes as they may have paid on income, in fact and in truth the income of the respective trusts but nevertheless credited to them for income tax purposes; and

Whereas, it was the intention of all the parties hereto in participating in the said "Copartnership" that each copartner thereof should bear the burden of income taxes on the share of copartnership income to which each partner would be entitled, and the "Copartnership" can be continued on no other basis;

Now, Therefore, It Is Hereby Agreed:

Article I.

I.1. Beginning as of the first year in which the "Co-partnership" was in existence and continuing thereafter so long as either of the said trusts remain existent, and also copartners in said "Copartnership", each trust shall advance and pay unto the trustor of that trust, in order that the trustor may pay the taxes on what is in truth and in fact the income and the taxes of the trust out of and from its assets, a sum equal to the amount of income taxes, including any interest or penalties thereon,

Plaintiffs' Exhibit No. 16—(Continued)

which have been, are or shall hereafter be assessed against the respective trustor by the United States or any State or territory thereof, or be payable by him by reason of said Government crediting to him for tax purposes, the income which, in truth and in fact, was, is and will be the income of the said trust as copartner of said "Copartnership", and the income taxes which are in truth and in fact taxes of said trust.

I.2. If either trustor shall be required to pay income taxes on any payment made to him pursuant to the terms of division 1 of this Article I, then the respective trust shall pay that trustor, out of and from the assets of each, a sum equal to such payment.

I.3. In determining the sum equal to taxes paid by either trustor for the purposes of the foregoing divisions of this Article I, all taxes shall be computed according to the rate at which the income of the respective trusts would have been taxed had they each paid their own taxes on the share of the copartnership income to which each is, was or may be entitled by the terms of said Articles.

Article II.

Should the United States or any state or territory thereof hereafter refund to either trustor any of the taxes paid by him on income credited to him for tax purposes, which was in truth and in fact the income of the trust of which he is trustor, that trustor shall pay therefrom unto that trust a sum

Plaintiffs' Exhibit No. 16—(Continued)

equal to all taxes, including interest and penalties thereon, assessed against or payable by the said trust for each year as to which that trustor shall have received such refund; such payments to be at least equal to all sums paid or payable to that trustor by that trust hereunder.

Article III.

Nothing herein shall be deemed to be a statement or admission by the parties hereto that any income of the said trusts, or either of them, on account of the said "Copartnership", or otherwise, is properly, legally or otherwise owned by or taxable to either trustor, nor that said "Copartnership" is not a valid, bona fide partnership existing under and by virtue of the Articles of said "Copartnership", by reason whereof each of said trusts is entitled to the percentage of the net income of said "Copartnership", as by said Articles provided.

Article IV.

Throughout this Agreement, the singular shall include the plural and the plural shall include the singular; the masculine shall include the feminine and neuter genders, the feminine shall include the masculine and neuter genders, and the neuter shall include the masculine and female genders.

Article V.

This Agreement is executed in six (6) parts; each part is hereby declared to be an original; all, however, shall constitute but one and the same Agreement.

Plaintiffs' Exhibit No. 16—(Continued)

In Witness Whereof, the parties hereto have hereunto set their hands and seals as of the day and year first above written.

/s/ By JACK SMITH
/s/ By ROSE MAE SMITH

Barbara Ann Smith Trust, a Voluntary Express Trust
/s/ By JACK SMITH, Trustee.

Howard Samuel Smith Trust, a Voluntary Express Trust
/s/ By ROSE MAE SMITH, Trustee.

PLAINTIFFS' EXHIBIT No. 17

Boston Shoe Company

CONDENSED BALANCE SHEET
As of September 30, 1943

Assets

Cash	50.00	
Accounts Receivable	130,232.93	
Notes Receivable	1,997.95	
Merchandise Inventory	171,161.59	
Fixed	2,541.55	
Other	722.95	
Total Assets		306,706.97

Liabilities and Capital

Liabilities:		
Bank Overdraft	17,516.64	
Other	41,534.68	59,051.32
Capital—Jack Smith		247,655.65
Total Liabilities and Capital		306,706.97

PLAINTIFFS' EXHIBIT No. 18

BOSTON SHOE COMPANY
CONDENSED BALANCE SHEETS

October 1, 1943 to June 30, 1948

	As of October 1, 1943	As of December 31, 1943	As of December 31, 1944	(Admission of New Partner) As of January 1, 1945	As of December 31, 1945	As of December 31, 1946	As of December 31, 1947	As of June 30, 1948
ASSETS								
Cash	50.00	4,823.50	73,088.83	73,088.83	44,875.23	110,968.90	75.00	5,329.53
Receivable—Partner (Herman Weisbaupt)	.....	.....	.....	22,200.00	.....	.....	.....	.....
Receivable—Trade	132,230.88	104,427.81	80,258.25	76,739.39	67,518.99	94,388.17	144,372.13	180,085.36
Investments	.....	.....	25,000.00	25,000.00	125,828.12	126,059.89	101,337.50	100,000.00
Prepayment on Merchandise Purchase	.....	.....	200.00	.....	42,498.79	.....	.....	.....
Inventory	171,161.59	219,013.98	129,605.23	97,487.16	72,238.70	141,031.33	359,637.35	216,216.87
Fixed Assets	2,541.55	2,371.06	1,689.10	1,689.10	3,445.35	5,991.69	7,724.40	9,212.12
Other Assets	722.95	1,403.20	1,629.39	1,629.39	2,784.80	2,135.76	1,307.32	2,711.46
Total Assets	306,706.97	332,039.55	311,470.80	297,833.87	359,189.98	480,575.74	614,453.70	513,555.34
LIABILITIES AND CAPITAL								
Current Liabilities	59,051.32	61,777.31	40,881.98	5,045.05	44,860.33	51,018.68	285,180.28	154,854.70
Loans Payable to Partners	(a) 47,655.65	(a) 38,141.46	(a) 3,043.12	(b) 70,588.82	.....	.....	.....	.....
Capital	200,000.00	232,120.78	267,545.70	222,200.00	314,329.65	429,557.06	329,273.42	358,700.64
Total Liabilities and Capital	306,706.97	332,039.55	311,470.80	297,833.87	359,189.98	480,575.74	614,453.70	513,555.34

Notations:

(a) Jack Smith

(b) Jack Smith 29,793.80
Rose Smith 11,624.46
Howard Smith Trust 14,585.28
Barbara Ann Smith Trust 14,585.28

70,588.82

PLAINTIFFS' EXHIBIT No. 19

BOSTON SHOE COMPANY

ANALYSIS OF PARTNERS' CAPITAL ACCOUNTS

October 1, 1943 to June 30, 1948

Date		Jack Smith		Rose Smith		Howard S. Smith Trust		Barbara Ann Smith Trust		Herman Weishaupt		Total Capital
		Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	
10/ 1/43	Balance		80,000.00		60,000.00		30,000.00		30,000.00			200,000.00
12/31/43	Net Profit 10/ 1/43-12/31/43		13,891.77		10,418.83		5,209.41		5,209.41			
	Drawings			2,608.64								
	Balance		93,891.77		67,810.19		35,209.41		35,209.41			232,120.78
12/31/44	Net Profit 1/1/44-12/31/44		38,790.79		29,093.10		14,546.54		14,546.54			
	Drawings	25,931.88		25,278.83		5,170.67		5,170.67				
	Balance		106,750.68		71,624.46		44,585.28		44,585.28			267,545.70
1/ 1/45	Admittance of new partner										22,200.00	
	Excess of old capital over new capital transferred to loans payable and made available for withdrawal by old partners	26,750.68		11,624.46		14,585.28		14,585.28				
	Balance—new partnership		80,000.00		60,000.00		30,000.00		30,000.00		22,200.00	222,200.00
12/31/45	Net Profit 1/1/45-12/31/45		42,199.93		31,649.95		15,824.97		15,824.97		11,722.21	
	Drawings	7,657.91		6,390.96		3,669.59		3,669.59		3,704.33		
	Balance		114,542.02		85,258.99		42,155.38		42,155.38		30,217.88	314,329.65
12/31/46	Net Profit 1/1/46-12/31/46		77,463.23		58,097.42		29,048.71		29,048.71		21,517.57	
	Drawings	37,136.24		31,014.92		5,731.83		5,737.76		20,327.48		
	Balance		154,869.01		112,341.49		65,472.26		65,466.33		31,407.97	429,557.06
12/31/47	Reduction of reserve for bad debts for calendar years 1943 and 1944 per revenue agent's report		4,452.61									
	Net Profit 1/1/47-12/31/47		19,174.93		14,381.20		7,190.60		7,190.60		5,326.37	
	Drawings	64,846.02		52,694.77		14,768.31		14,773.34		10,917.51		
	Balance		113,650.53		74,027.92		57,894.55		57,883.59		25,816.83	329,273.42
6/30/48	Net Profit 1/1/48-6/30/48		18,815.99		14,111.98		7,056.00		7,056.00		5,226.67	
	Drawings (incl. credits to trusts)	16,894.82		10,047.78			2,520.28		2,520.28	937.38		
	Balance		115,571.70		78,092.12		67,470.83		67,459.87		30,106.12	358,700.64

PLAINTIFF'S EXHIBIT No. 20

BOSTON SHOE COMPANY
ANALYSIS OF PARTNERS' DRAWING ACCOUNTS

October 1, 1943 to June 30, 1948

Year		Jack Smith	Rose Smith	Howard S. Smith Trust	Barbara Ann Smith Trust	Herman Weishaupt
1943	Income Taxes	.....	2,467.35	.....	.....	.....
	Personal	6,250.00	741.29	.....	.....	.....
		6,250.00	3,208.64	.....	.....	.....
	Less Salary	6,250.00	600.00	.....	.....	.....
	Net Drawings	.....	2,608.64	.....	.....	.....
1944	Income Taxes	.....	14,528.83	1,320.67	1,320.67	.....
	Personal and Misc.	50,931.88	13,150.00	100.00	100.00	.....
	Investments	.....	.....	3,750.00	3,750.00	.....
		50,931.88	27,678.83	5,170.67	5,170.67	.....
	Less Salary	25,000.00	2,400.00	.....	.....	.....
	Net Drawings	25,931.88	25,278.83	5,170.67	5,170.67	.....
1945	Income Taxes	4,798.67	5,299.11	3,669.59	3,669.59	704.33
	Personal	27,859.24	3,491.85	.....	.....	9,000.00
		32,657.91	8,790.96	3,669.59	3,669.59	9,704.33
	Less Salary	25,000.00	2,400.00	.....	.....	6,000.00
	Net Drawings	7,657.91	6,390.96	3,669.59	3,669.59	3,704.33
1946	Income Taxes	29,062.15	23,114.92	5,731.83	5,737.76	7,364.18
	Personal	33,074.09	10,300.00	.....	.....	18,963.30
		62,136.24	33,414.92	5,731.83	5,737.76	26,327.48
	Less Salary	25,000.00	2,400.00	.....	.....	6,000.00
	Net Drawings	37,136.24	31,014.92	5,731.83	5,737.76	20,327.48
1947	Income Taxes	73,051.61	52,029.57	12,268.31	12,273.34	8,194.32
	Personal	16,794.41	3,065.20	.....	.....	8,723.19
	Loan	.....	.....	2,500.00	2,500.00	.....
		89,846.02	55,094.77	14,768.31	14,773.34	16,917.51
	Less Salary	25,000.00	2,400.00	.....	.....	6,000.00
	Net Drawings	64,846.02	52,694.77	14,768.31	14,773.34	10,917.51
1948	Income Taxes	13,864.09	9,800.08	.....	.....	(
	Personal	15,530.73	1,447.70	.....	.....	3,937.38
	Repayment of Loan and Interest	.....	.....	(2,520.28)	(2,520.28)	)
		29,394.82	11,247.78	(2,520.28)	(2,520.28)	3,937.38
	Less Salary	12,500.00	1,200.00	.....	.....	3,000.00
	Net Drawings	16,894.82	10,047.78	(2,520.28)	(2,520.28)	937.38

PLAINTIFFS' EXHIBIT No. 21

SCHEDULE OF RECEIPTS-DISBURSEMENTS-INVESTMENTS
HOWARD SAMUEL SMITH TRUST
12/28/42 to 12/31/48

		Receipts	Disbursements
12/28/42	Gift from Jack and Rose Smith	$ 4,000.00	.....
	Interest 12/28/42 to 6/30/48	183.50	.....
9/28/43	Gift from Jack and Rose Smith	30,121.20	.....
	Misc. Savings and Interest 1/27/33-6/30/48	141.40	.....
12/31/43	Income Inv. Boston Shoe Co.—1943	5,209.41	.....
1944	Federal Income Tax Payments	.....	1,269.58
	Calif. State Income Tax Payments	.....	51.09
	Interest—Union Bank	1.65	.....
12/31/44	Income Inv.—Boston Shoe Co.—1944	14,546.54	.....
1945	Federal Income Tax Payments (¾)	.....	3,606.61
	Calif. State Income Tax Payments (⅓)	.....	62.98
	Federal Income Tax Payments (¼)	.....	1,202.20
	Calif. State Income Tax Payments (⅔)	.....	125.95
	Interest on Federal Tax	.....	.15
	Interest on State Tax	.....	.20
12/31/45	Income Inv—Boston Shoe Co.—1945	15,824.97	.....
1945	Interest Union Bank	55.98	.....
1946	Federal Income Tax Payments	.....	5,509.73
	Calif. State Income Tax Payments	.....	222.10
	Interest Union Bank	74.00	.....
12/31/46	Income Inv—Boston Shoe Co.—1946	29,048.71	.....
1947	Federal Income Tax Payments	.....	11,531.88
	Calif. State Income Tax Payments	.....	736.43
	Interest Union Bank	74.36	.....
12/31/47	Income Inv—Boston Shoe Co.—1947	7,190.60	.....
2/24/48	Interest—Loan to Ben Breiman	20.28	.....
6/30/48	Interest Union Bank	37.30	.....
6/30/48	Income Inv—Boston Shoe Co.—1948	7,056.00	.....
6/30/48	Tax Adjustment 10/1/43 to 12/31/47	.....	37,289.73
12/31/48	Interest Coast Fed. Sav. Bk.	74.79	.....
	Interest Republic Fed. Sav. Bk.	74.78	.....
	Interest Western Fed. Sav. Bk.	64.86	.....
7/ 9/48	Cash gift Jack and Rose Smith	.03	.....
	Totals	113,800.36	61,608.63
	Net Worth	.....	52,191.73
		113,800.36	113,800.36

Plaintiffs' Exhibit No. 21—(Continued)

SCHEDULE OF INVESTMENTS
HOWARD SAMUEL SMITH—TRUST
12/28/42 to 12/31/48

		Invest	Withdraw	Balance at 12/31/48
Union Bank & Trust Co. Savings:				
(½ Joint Acct. Howard and Barbara Smith)				
12/28/42	(Gift from J&R Smith)	4,000.00	.....	.....
	Interest 12/28/42 to 6/30/48	183.50	.....	.....
	6/30/48	.....	4,183.50	.....
	Misc. Deposits & Int. 1/27/33 to 6/30/48	141.40	.....	.....
	6/30/48	.....	141.40	.....
2/16/44	Tfr from B.S.C.	100.00	.....	.....
3/14/44	Tfr from B.S.C.	121.20	.....	.....
1944	Interest	1.65	.....	.....
2/20/45	Tfr from B.S.C.	14,585.28	.....	.....
6/13/45	(Fed. Inc. Tax Payment)	.....	1,202.35	.....
8/13/45	(Cal. St. Inc. Tax Payment)	.....	126.15	.....
1945	Interest	55.98	.....	.....
2/20/45	Purchase U. S. Sav. Bonds	.....	3,750.00	.....
1946	Interest	74.00	.....	.....
1947	Interest	74.36	.....	.....
6/30/48	Interest	37.30	.....	.....
7/ 9/48	Withdrawal	.....	9,971.27	.....
		15,049.77	15,049.77	.....
U. S. Savings Bonds				
9/28/43	Gift from J&R Smith	30,000.00	.....	.....
10/ 1/43	To Boston Shoe Co.	.....	30,000.00	.....
11/29/44	Series E U. S. Savings Bonds	3,750.00	.....	.....
2/20/45	Series E U. S. Savings Bonds	3,750.00	.....	.....
		37,500.00	30,000.00	7,500.00
11/ 6/47	Loan to Ben Breiman	2,500.00	.....	.....
2/28/48	Paid in full	.....	2,500.00	.....
Savings & Loan Accounts:				
7/10/48	Coast Fed. Sav. Bk.	4,985.65	.....	.....
	Interest to 12/31/48	74.79	.....	5,060.44
7/14/48	Republic Fed. Sav. & Loan	4,985.65	.....	.....
	Interest to 12/31/48	74.78	.....	5,060.43
7/12/48	Western Fed. Sav. & Loan	4,324.90	.....	.....
	Interest to 12/31/48	64.86	.....	4,389.76
Investment—Boston Shoe Co.:				
10/ 1/43	Investment	30,000.00	.....	.....
	1943 Share of Profits	5,209.41	.....	.....
2/16/44	Cash drawing (Dep. Union Bank)	.....	100.00	.....
11/29/44	Cash drawing (U. S. Bonds)	.....	3,750.00	.....
1944	Fed. Inc. Tax Paid	.....	1,269.58	.....
1944	Cal. Inc. Tax Paid	.....	51.09	.....
	1944 Share of Profits	14,546.54	.....	.....
2/20/45	Cash drawing (Dep. Union Bank)	.....	14,585.28	.....
1945	Fed. Inc. Tax Paid	.....	3,606.61	.....
	Cal. Inc. Tax Paid	.....	62.98	.....
	1945 Share of Profits	15,824.97	.....	.....
1946	Fed. Inc. Tax Paid	.....	5,509.73	.....
	Cal. Inc. Tax Paid	.....	222.10	.....
	1946 Share of Profits	29,048.71	.....	.....
1947	Fed. Inc. Tax Paid	.....	11,531.88	.....
	Cal. Inc. Tax Paid	.....	736.43	.....
11/ 6/47	Cash drawing (Loan to Ben Breiman)	.....	2,500.00	.....
	1947 Share of Profits	7,190.60	.....	.....
6/30/48	1948 Share of Profits	7,056.00	.....	.....
2/24/48	Ret of Loan and Int. from Breiman	2,520.28	.....	.....
6/30/48	Tax Adjustment 10/1/43 to 12/31/47	.....	37,289.73	.....
		111,396.51	81,215.41	.....
Boston Shoe Co. Total Investment				30,181.10
Total Investments as at 12/31/48				$ 52,191.73

PLAINTIFFS' EXHIBIT No. 22

SCHEDULE OF RECEIPTS—DISBURSEMENTS
BARBARA ANN SMITH TRUST
12/28/42 to 12/31/48

		Receipts	Disbursements
12/28/42	Gift from Jack and Rose Smith	$ 4,000.00	.....
	Interest 12/28/42 to 6/30/48	183.51	.....
9/28/43	Gift from Jack and Rose Smith	32,250.00	.....
12/31/43	Income Inv—Boston Shoe Co.—1943	5,209.41	.....
1944	Federal Income Tax Payments	.....	1,269.58
	Calif. State Income Tax Payments	.....	51.09
	Interest—Union Bank	6.62	.....
12/31/44	Income Inv—Boston Shoe Co.—1944	14,546.54	.....
1945	Fed. Income Tax Payments (3/4)	.....	3,606.61
	Calif. State Income Tax Pay (1/3)	.....	62.98
	Fed. Income Tax Payments (1/4)	.....	1,202.20
	Calif. State Income Tax Pay (2/3)	.....	125.95
	Interest on Fed. Tax	.....	.15
	Interest on State Tax	.....	.20
12/31/45	Income Inv—Boston Shoe Co.—1945	15,824.97	.....
1945	Interest Union Bank	67.51	.....
1946	Federal Income Tax Payments	.....	5,515.32
	Calif. State Income Tax	.....	222.44
	Interest Union Bank	82.27	.....
12/31/46	Income Inv—Boston Shoe Co.—1946	29,048.71	.....
1947	Federal Income Tax Payments	.....	11,536.49
	Calif. State Income Tax	.....	736.85
	Interest Union Bank	82.62	.....
12/31/47	Income Inv—Boston Shoe Co.—1947	7,190.60	.....
2/24/48	Interest—Loan to Ben Breiman	20.28	.....
6/30/48	Interest Union Bank	41.43	.....
6/30/48	Income—Inv—Boston Shoe Co.—1948	7,056.00	.....
6/30/48	Tax Adjustment 10/1/43 to 12/31/47	.....	31,480.20
12/31/48	Interest Coast Fed. Sav. Bk.	60.00	.....
	Interest Home Bldg. & Loan Assoc.	60.00	.....
	Interest Los Angeles Fed. Sav. Bk.	62.06	.....
	Interest Standard Fed. Sav. Bk.	62.75	.....
7/ 9/48	Cash gift Jack and Rose Smith	.06	.....
	Total	115,855.34	55,810.06
	Net Worth	.....	60,045.28
		115,855.34	115,855.34

Plaintiffs' Exhibit No. 22—(Continued)

SCHEDULE OF INVESTMENTS
BARBARA ANN SMITH—TRUST
12/28/42 to 12/31/48

		Invest	Withdraw	Balance at 12/31/48
Union Bank & Trust Co. Savings:				
(½ Joint Acct. Howard & Barbara Smith)				
12/28/42	(Gift from J&R Smith)	4,000.00	.....	.....
	Interest 12/28/42 to 6/30/48	183.51	.....	.....
6/30/48	Withdrawal	.....	4,183.51	.....
2/16/44	Tfr from B.S.C.	100.00	.....	.....
3/14/44	Tfr from B.S.C.	2,250.00	.....	.....
1944	Interest	6.62	.....	.....
2/20/45	Trf from B.S.C.	14,585.28	.....	.....
2/20/45	Purchase U. S. Sav. Bonds	.....	3,750.00	.....
6/13/45	Fed. Inc. Tax Payment	.....	1,202.35	.....
8/13/45	Cal. State Inc. Tax Payment	.....	126.15	.....
1945	Interest	67.51	.....	.....
1946	Interest	82.27	.....	.....
1947	Interest	82.62	.....	.....
6/30/48	Interest	41.43	.....	.....
7/ 9/48	Withdrawal	.....	12,137.23	.....
		17,215.73	17,215.73	.....
U. S. Savings Bonds:				
9/28/43	Gift from J&R Smith	30,000.00	.....	.....
10/ 1/43	To Boston Shoe Co.	.....	30,000.00	.....
11/29/44	Series E U. S. Savings Bonds	3,750.00	.....	.....
2/20/45	Series E U. S. Savings Bonds	3,750.00	.....	.....
		37,500.00	30,000.00	7,500.00
11/ 6/47	Loan to Ben Breiman	2,500.00	.....	.....
2/28/48	Paid in full	.....	2,500.00	.....
Savings & Loan Accounts:				
7/10/48	Coast Fed. Sav. & Loan Assoc.	4,000.00	.....	.....
	Interest to 12/31/48	60.00	.....	4,060.00
7/10/48	Home Bldg. & Loan Assoc.	4,000.00	.....	.....
	Interest to 12/31/48	60.00	.....	4,060.00
7/10/48	Los Angeles Fed. Sav.	4,137.30	.....	.....
	Interest to 12/31/48	62.06	.....	4,199.36
7/12/48	Standard Fed. Sav. & Loan Assoc.	4,183.50	.....	.....
	Interest to 12/31/48	62.75	.....	4,246.25
Investment—Boston Shoe Co.:				
10/ 1/43	Investment	30,000.00	.....	.....
	1943 Share of Profits	5,209.41	.....	.....
2/16/44	Cash Draw (Dep. Union Bank)	.....	100.00	.....
1944	Fed. Inc. Tax Paid	.....	1,269.58	.....
	State Inc. Tax Paid	.....	51.09	.....
11/29/44	Cash Draw (U. S. Bonds)	.....	3,750.00	.....
	1944 Share of Profits	14,546.54	.....	.....
2/20/45	Cash Draw (Dep. Union Bank)	.....	14,585.28	.....
1945	Fed. Inc. Tax Paid	.....	3,606.61	.....
	State Inc. Tax Paid	.....	62.98	.....
	1945 Share of Profits	15,824.97	.....	.....
1946	Fed. Inc. Tax Paid	.....	5,515.32	.....
	State Inc. Tax Paid	.....	222.44	.....
	1946 Share of Profits	29,048.71	.....	.....
1947	Fed. Inc. Tax Paid	.....	11,536.49	.....
	State Inc. Tax Paid	.....	736.85	.....
11/ 6/47	Cash Draw (Loan to Ben Breiman)	.....	2,500.00	.....
	1947 Share of Profits	7,190.60	.....	.....
2/24/48	Ret. of Loan & Int. from Breiman	2,520.28	.....	.....
6/30/48	1948 Share of Profits	7,056.00	.....	.....
6/30/48	Tax Adjustment 10/1/43 to 12/31/47	.....	31,480.20	.....
		111,396.51	75,416.84	.....
Boston Shoe Co. Total Investment				35,979.67
Total Investment 12/31/48				$ 60,045.28

[Endorsed]: No. 14594. United States Court of Appeals for the Ninth Circuit. Jack Smith and Rose Mae Smith, Appellants, vs. Harry C. Westover, former Collector of Internal Revenue, and Robert A. Riddell, Director of Internal Revenue, Appellees. Transcript of Record. Appeal from the United States District Court for the Southern District of California, Central Division.

Filed: December 9, 1954.

/s/ PAUL P. O'BRIEN,
Clerk of the United States Court of Appeals for the Ninth Circuit.

In the United States Court of Appeals
for the Ninth Circuit

No. 14594

JACK SMITH and ROSE MAE SMITH,
Appellants,

vs.

HARRY C. WESTOVER, former Collector of Internal Revenue, and ROBERT A. RIDDELL, Director of Internal Revenue,
Appellees.

APPELLANTS' STATEMENT OF POINTS AND DESIGNATION OF RECORD

Statement of Points

The appellants hereby state that they intend to rely on appeal upon the following points:

1. The District Court erred in ordering judgment for the defendants.

2. The District Court erred in adopting the findings of fact and conclusions of law filed by the defendants.

3. The District Court erred in adopting the judgment, docketed and entered on August 23, 1954

4. The District Court erred in denying plaintiffs motions to amend findings and judgment and for a new trial.

5. The District Court erred in failing to find as a fact that the partnership involved herein was at all times a bona fide partnership entitled to full recognition for Federal income tax purposes.

6. The District Court erred in failing to enter judgment for the plaintiffs.

Designation of Record to be Printed

Pursuant to rule 17(6) of this Court, appellants hereby designate the following parts of the record as being necessary for consideration of the points upon which they intend to rely on this appeal, and desire to have printed, omitting the title of Court and cause from each of the documents designated for printing:

1. The complete record certified by the Clerk of the District Court to the Court of Appeals.

2. The District Court Clerk's certification of Record on Appeal.

3. This Statement of Points and Designation of Record on Appeal.

Dated: December 15, 1954.

Respectfully submitted,

LATHAM & WATKINS,
/s/ By DANA LATHAM,
/s/ By HENRY C. DIEHL

Affidavit of Service by Mail attached.

[Endorsed]: Filed December 17, 1954. Paul P. O'Brien, Clerk.